

***United States Court of Appeals  
for the Second Circuit***



**JOINT APPENDIX**



76-7278

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United States Court of Appeals

FOR THE SECOND CIRCUIT

Docket No. 76-7278

MARGARET MARY McDONNELL MURPHY,

*Plaintiff-Appellant.*

*against*

McDONNELL & CO., INCORPORATED and  
THE NEW YORK STOCK EXCHANGE by

ROBERT W. HAACK, President,

*Defendants.*

B

JAMES F. McDONNELL, JR., individually, as Trustee under the Will of James F. McDonnell and as Executor of the Estate of Anna M. McDonnell, and CHARLES E. McDONNELL, as Executor of the Estate of Anna M. McDonnell,  
*Plaintiff-Appellants,*  
*against*

THE NEW YORK STOCK EXCHANGE by ROBERT W. HAACK, THE NEW YORK STOCK EXCHANGE, INC., THE AMERICAN STOCK EXCHANGE by H. VERNON LEE, JR., Secretary, and McDONNELL & CO., INC.,  
*Defendants.*

ON APPEAL FROM THE UNITED STATES DISTRICT COURT  
FOR THE SOUTHERN DISTRICT OF NEW YORK

JOINT APPENDIX

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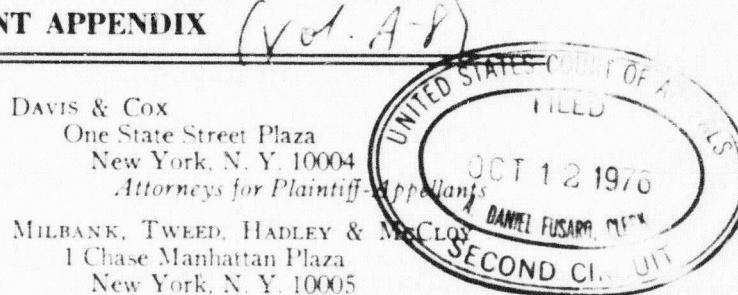
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October 8, 1976.



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## AFTERNOON SESSION

1:10 P.M.

(In the courtroom in the presence of the jury.)

## CHARGE OF THE COURT

(Owen, J.)

THE COURT: Madam forelady and ladies and gentlemen of the jury:

As someone said in the Bible, better the beginning of the end than the end of the beginning. We are at the beginning of the end.

We are now at that stage of the trial where you are about to undertake your final functions as jurors here, and in doing so, as I suggested to you at the time you were selected, you will be performing one of the most valued and responsible obligations of citizenship, which is to act as ministers of justice here and to decide the facts in this controversy between fellow citizens.

Now while the evidence in this case is probably clear in your minds, in preparing this charge I concluded that my instructions to you in these circumstances got me into certain complexities in my assisting you in your function, and in order, therefore, to enable you to perform that function as effectively as possible as jurors with the greatest possible clarity on the law that you would be

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applying to what you are going to have to do, I am going to divide your deliberations into two parts. I shall charge you now generally on many matters that apply to your entire deliberations, and I will specifically charge you now on the law under which you shall determine whether any defendant is liable to any plaintiff on any claim. In other words, I am going to ask you first to make a determination on the liability here that is asserted.

In the event, and only in the event, that you do find liability on the part of any plaintiff against any defendant on any claim, then and only then will I instruct you on the rules of law under which you shall determine damages flowing, if any, from such liability.

Obviously, if you find no liability in any case, there is no basis for thereafter determining damages.

Now, you are to discharge your final duty as jurors here in an attitude of complete fairness, complete impartiality, and, as I am sure you remember my emphasizing when you were selected, with complete absence of bias or prejudice for or against any party to this controversy.

All parties, whether individuals, partnerships or corporations, stand as equals before you and before the law, and are to be dealt with as equals in a court of justice.

Thus, the fact that certain plaintiffs are individuals while the defendant McDonnell & Co. is a corporation now in receivership, should in no way affect your verdict or influence your deliberations. You are to treat them equally.

Your final role is to decide and pass upon the fact issues. You are the sole and exclusive judges of those facts. You are to determine the weight of the evidence; you are to appraise the credibility or truthfulness of the witnesses; you are to draw such reasonable inferences from the evidence as you feel are warranted; you are to resolve such conflicts as you may find exist in the evidence before you.

I shall tell you later how to go about determining credibility of witnesses, or give you factors which will assist you in that regard.

You are to decide this case on the evidence presented here in this courtroom and on that evidence alone. That includes the testimony and the exhibits, or the lack of evidence, as the case may be. But in all things, in all your deliberations, as I told you at one point early in the trial, you do not leave your common sense in the hallway. You apply it at every stage.

Now, my final function is to instruct you as to

the law to apply in this situation, and it is your duty to accept these instructions as to the law and to apply them to the facts as you may find them to be.

Now, you are not to consider any one instruction which I give you standing alone as stating the law. You should take all of my instructions together as an entire whole.

With respect to any fact matter which I mentioned to you during the summations, is your recollection and yours alone that governs.

Anything that any attorney may have said with respect to matters in evidence, whether during the trial, in questions, in argument or in summation is not to be substituted for your recollection of the evidence.

So, too, anything that I might say or might have said during the trial, or anything I might refer to during the course of these instructions with regard to any matter in evidence is not to be taken in lieu of your own recollection.

Now, when attorneys on both sides have stipulated or conceded or agreed to the existence of a fact, you should accept the correctness of that fact and treat it as proved. Questions are not evidence. It is the answer which constitutes the evidence.

Now, the attorneys not only had the right but the duty to make objections and press legal theories with regard to questions. Therefore, any evidence as to which an objection was sustained by the court and any answer which was stricken is to be disregarded by you, and you are to hold nothing against any lawyer for exercising the right to object to any question or make any legal argument that is appropriate.

As I said, you and you alone are the finders of the fact here. We are not. Do not assume that I hold any opinion on any matters concerning this case, and do not reach any conclusion that I lean one way or the other. I do not.

A word about the testimony from depositions: during the trial I think two sides read to you testimony by way of depositions taken prior to trial. That is where the witness was questioned by the lawyers out of court and the testimony signed and sworn to before a notary public. This is perfectly permissible. Testimony given to you in that fashion is entitled to the same consideration on your part as if the witness had been here in the courtroom and had testified from the witness stand, and you are to weigh that evidence and treat it in just the same manner as if it were live testimony.

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Now this is a civil case. In a civil case where there are four plaintiffs, each plaintiff has the burden of proof to establish all the elements of that party's case against a defendant sought to be made responsible, and has the burden of proving that by a preponderance of the credible evidence.

Now, to determine whether a plaintiff has met the burden of proving his or her case by a preponderance of the credible evidence, you should take all of the evidence in your mind, that which supports that party's contention against that which supports opposing contentions, and you should then determine which is the more convincing, which is probably the more correct version of the facts, which seems to you to make more sense, which is more likely so than not so. This does not mean you should add up the number of witnesses on each side and actually balance them. You, the jury, are interested not in the quantity of evidence but, obviously, the quality of the evidence that you have heard. Which evidence do you find is more likely to represent the true picture of what actually happened?

Should there be conflicting evidence and should it be evenly balanced in your mind so that you are unable to say that the evidence on either side of an issue preponderates, then your finding must be against the plaintiff

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who carries the burden of proof on that issue.

If you can imagine in your minds the scales of justice, then the party who has the burden of proof must tip that scale slightly in his or her favor. If the scales remain evenly balanced, or if it tips down on the defendant's side on that issue, then the plaintiff carrying the burden of proof on that issue has not sustained that burden, and you are therefore to find that the plaintiff has not met his burden of proof on that issue.

Now, the facts in this case may be proved by either direct or by circumstantial evidence. It must be by one or the other.

Direct evidence is where a witness testifies to what he or she saw, heard, smelled, felt. It is an immediate reaction to something. It is testimony of what one observed with one's senses.

Circumstantial evidence is where facts are established from other facts which are properly proved for you and from which you may logically infer the final facts sought to be established.

Thus, you go on the basis of reason and experience from an established fact to the next fact to be proved.

Circumstantial evidence, if you credit it, is of no less value than direct evidence.

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To give you a homely example that I have heard repeated by countless judges over years at the bar and have used myself, it is roughly as follows: Let's suppose you come in this morning and the blinds are drawn. It has been a sunny day when you came in. As you sit here during the middle of the morning a man comes in with a raincoat with drops of water on it. Another man comes in with an umbrella and he shakes the water off it and he puts it up against the wall. You could conclude from those facts that since you had come into the building the sun had stopped shining and it had started to rain. That's what is meant by circumstantial evidence. You go from one established fact to the next one which logically, and reasonably follows.

Now let's go to one of your major functions in deciding issues of fact. That is, how do you determine the credibility or believability of witnesses who have testified before you and determining the weight to be given to their testimony.

As I have said, you heard considerable testimony in this case. Some of it is in conflict. How do you resolve that conflict? How do you determine the weight to be given to the testimony of a given witness? How do you determine if he or she is credible or believable?

Among other things, and at the outset in your search for truth, you use your plain everyday common sense. You have seen the witness; you have heard his or her testimony; you have observed the witness' demeanor. How did the witness impress you? Did the witness appear to be testifying frankly, candidly, fairly? In other words, in evaluating the testimony and the believability you apply your common sense and experience exactly as you would do in determining an important matter in your own life.

You should consider, as I am sure you will, the witness' demeanor, background, candor, lack of candor, possible bias, means of information, accuracy of recollection and probably a lot of other things along the same line.

You should consider whether a witness' testimony is supported by - that is, corroborated by any other evidence in the case, whether it is contradicted by believable and credible evidence elsewhere in the case.

If you find that a witness has made a material misstatement of fact with the intention of misleading you, you may disregard that portion of the witness' testimony which you do not believe, or you may disregard all of it; or you may accept that part which you find reliable and disregard the rest of it.

Even though the testimony of a witness is

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uncontradicted you are not compelled to accept it. You may accept it or reject it depending on whether or not it commands itself to you, taking into account, among other things, the demeanor of the witness & the stand and the impression that that witness made upon you.

Now may I say that you are aware that Mr. Murray McDonnell has not testified in this case. Since there is no evidence that his testimony was not equally available to all parties, I charge you that you may draw no inference for or against any party for Mr. Murray McDonnell's non-appearance on this trial.

We had a gentleman, a Professor Ratner, who testified as to an opinion on certain subjects. Normally, as I think you are beginning to sense, the rules of evidence do not generally permit a witness to testify as to an opinion. A so-called expert witness is an exception to this general rule. Such a person is really nothing more than one who has become expert in a given profession and is therefore permitted to state an opinion as to matters as to which he is presumably versed and which are material to the issues in the case. He may also a basis or a reason for opinion evidence.

Nevertheless, ladies and gentlemen, just because a man is called an expert does not mean that you are obliged

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to accept his opinion or follow his view. Quite to the contrary. You are entitled to accept or reject opinion, evidence given by an expert depending on how you assess his statements, the opinions and the reasons he gave for it. In other words, you evaluate him in the same way as you would evaluate any other witness.

All of the plaintiffs and the officers and employees of the defendant McDonnell Company and the stock exchange -- actually, with regard to McDonnell & Company it was only the receiver -- certain employees of the stock exchange have given testimony in this trial.

Now, because McDonnell and the stock exchange are parties to this action, their representatives, their employees and their officers are what we call interested witnesses. That is, they have or may have some interest in the outcome of the trial. And the same is obviously true with respect to each of the plaintiffs in this case. That is, Mrs. Murphy, Mr. James McDonnell and Mrs. Anna McDonnell and the McDonnell trust in the name of the deceased father.

Now, the fact that a witness has an interest in the outcome of the case does not necessarily mean that that witness has not told the truth. It is for you to determine from your observation of his or her demeanor on the stand, you using your common sense and experience and

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all of the other considerations that I previously gave you, to determine whether or not the possible interest of any witness in the outcome of the lawsuit is such that he or she is likely, intentionally or otherwise, to have colored testimony.

You may, if you deem it proper under all the circumstances, disbelieve the testimony of such an interested witness, even though it is not otherwise impeached or contradicted.

However, you are not required to disbelieve such a witness merely because of possible interest in the outcome, and you may accept all or such parts of such witness' testimony as you deem reliable, and you should reject such part as you deem unworthy of acceptance.

Now, there are three individual and one organizational type of plaintiffs suing the defendants in this case. For convenience all of these issues are being tried together, but each of the various plaintiffs' claims must be considered separately by you in your deliberations. This is not an overall lumping of things together.

Now, as I said earlier, but I will repeat, the four plaintiffs are Mrs. Murphy, Mr. James McDonnell, Mrs. Anna McDonnell and the trust of James McDonnell, Sr.

Mrs. Murphy is suing for damages she claimed occurred

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because of the fraud on McDonnell & Company.

Now, in connection with this I want to say that McDonnell & Company is now in receivership, and a Mr. Stargatt is the receiver, as you heard when he testified here, but throughout my charge I generally refer to the firm as McDonnell & Company whether it is before or after.

She claims that there is a fraud on the part of McDonnell & Company in causing her to put certain of her property into McDonnell in late January or early February, 1969.

She also claims that the New York Stock Exchange failed to properly regulate McDonnell & Company, leading, she claims to its demise and her loss of her investment.

The second plaintiff, Mrs. Anna McDonnell, is suing for damages for fraud allegedly perpetrated on her by McDonnell & Company in getting her to add property to an already subordinated account in the year 1969. That's against McDonnell.

She alleges the same failure of the stock exchange to regulate, the same as her daughter did, and claims that that caused the loss of her property so put into the company.

James McDonnell is suing McDonnell & Company for the value of certain common stock that you heard him testify he bought in order to qualify to become a branch manager

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in Detroit in the spring of 1969.

He claims that there were omissions in what the people in the company told him about its condition, or he wouldn't have put the money in. He asserts that he was defrauded.

He too claims that if the stock exchange -- this is his claim against the stock exchange-- he claims that if the stock exchange had properly regulated it he would not have lost this investment.

The trust, which is the fourth of the plaintiffs, the trust of the father, has two claims. One is against both defendants and one is only against the stock exchange. The one that is against both defendants involves the claim in connection with the roll over of a Series B debenture at the end of December, 1968.

It is asserted that the roll over was procured by the fraud of Murray McDonnell on behalf of the company who, in his capacity as a trustee, executed an instrument causing the roll over, whereas under the trust agreement they needed at least two of the three trustees' signatures.

It is asserted that he did this as the chief executive of McDonnell in order to keep the funds in the company. That's a claim against McDonnell.

The claim against the stock exchange is the same

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one as before, that the stock exchange failed to supervise McDonnell & Company itself and that it went into receivership and causing the rolled over debenture to become worthless.

Now Mr. Beebe argued to you the fact that the stock exchange had a duty to see to it that there were the proper signatures on the authorizations for the Series E debenture and the roll over. In thinking back on it I did not express myself well in certain earlier rulings of law I had made in this case, because at that time I had intended to convey, and I obviously did not, I intended to convey, and I state to you as a jury, I do not find any basis for a requirement that the New York Stock Exchange check out the number of signatures of trustees to the roll over in the face of the fact of the Lybrand audit, which was a major auditing company in this city, and their certificate that everything was in order.

I therefore withdraw that aspect of the case from your consideration.

So the contention that is being submitted to you is whether the New York Stock Exchange's failure to supervise caused the loss of value of the roll over debenture.

The second claim of the trustee which is asserted against the New York Stock Exchange is that at some time

during Father McDonnell's life he had owned certain preferred stock which found its way into the trust which you have heard a lot of testimony about, and it was in that trust, and the claim is that if the stock exchange had properly regulated McDonnell & Company it would not have gone out of business and that security would not have become valueless.

Now, these claims are all vigorously denied, as you have heard over three weeks plus of testimony here, denied and disputed. It is those facts that you are going to have to resolve: Four claims of the plaintiffs against McDonnell & Company and the five claims of the plaintiffs against the New York Stock Exchange. So you must consider each one separately.

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The mere fact that a plaintiff may have suffered a loss in connection with an investment does not in and of itself entitle that plaintiff to recover from any defendant nor does that fact in and of itself make any defendant liable to a plaintiff, nor is any defendant an insurer of a plaintiff's loss.

You may not find for a plaintiff just because one event preceded another or followed another. In order to prevail under any theory, the plaintiff must prove to your satisfaction by a preponderance of the credible evidence each element of his or her claim or theory.

Now I propose to set forth for you what the elements are that are required for the plaintiff to prove in any case, and explain to you what is involved in each element.

If a plaintiff has proved each element of that claim to your satisfaction by a fair preponderance of the evidence, then as to that claim your verdict must be for the plaintiff on liability. If any plaintiff has failed in such proof as to any claim, then your verdict would be for the defendant on that claim. In no event, ladies and gentlemen, are you to guess, to speculate, to conjecture or to surmise. Obviously,

you may not base a verdict upon a guess, speculation, conjecture or surmise.

Now, Congress has enacted laws designed to protect the investing public. The laws require full disclosure of all material facts about securities offered for sale. This is to give the investing public access to information necessary to make a realistic and informed decision about what they are putting their money in, its merits, and thus to exercise an informed judgment in determining whether or not to buy it. The Congress has also enacted other laws concerning the marketplace and its regulation where these investors buy and sell.

Section 10B of the Securities Act of 1934 and rule 10B5, which is promulgated under that statute, are prominently featured in what you are going to have to consider.

As I have said, the complaints allege that the subordination agreement of Mrs. Murphy and of Mrs. Anna McDonnell and James McDonnell's purchase of common stock and the rollover of the series B subordinated debentures owned by the trust are alleged against McDonnell & Company as violations of section 10B and rule 10B5.

Section 10B provides in pertinent part as

follows:

"It shall be unlawful for any person" -- and that includes a corporation -- "directly or indirectly, by use of any means or instrumentality of interstate commerce or of the mails or of any facility of any national securities exchange to use or employ in connection with the purchase or sale of any security any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the commission may prescribe as necessary or appropriate in the public interest or for the protection of investors."

I am going to explain that to you a little bit further on, so we are not going to be dealing with that language alone.

Among the rules adopted by the Securities and Exchange Commission pursuant to the authority granted by this section is rule 10B5. That provides:

"It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails, or of any national securities exchange, to employ any device, scheme, or artifice to defraud.

"2: To make any untrue statement of a material fact or to omit to state a material fact

necessary in order to make the statements made in the light of the circumstances under which they were made not misleading or

"3: To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person in connection with purchase or sale of any security."

Now, the 10B and 10B5 claims are only against McDonnell. In order to find McDonnell liable for violation of rule 10B5 in connection with any of the first three transactions -- and I am going to put to one side the debenture rollover because it requires a little special treatment under the law -- but with regard to either of subordination agreements of Mrs. Murphy or her mother or the stock purchase of James McDonnell, you must be satisfied that as to the particular transaction plaintiff involved has established each of the following essential elements by a fair preponderance of the credible evidence:

First, the particular transaction you are considering was in connection with, that is, involved a purchase or sale of a security.

In this connection, I instruct you that stocks, common stocks such as James McDonnell bought

and the subordination agreements that Mrs. Murphy and her mother received, are securities for purposes of rule 10B5, and therefore if you find that plaintiff entered into such an agreement -- and there doesn't seem to be any dispute as to the instrument -- then that plaintiff has purchased a security, and that element is satisfied.

Second, you must find that the representations that were made by McDonnell & Company through an officer, agent or otherwise, attributable to McDonnell, that the representations contained untrue statements of fact, or that McDonnell & Company omitted to state facts necessary in order to make the statements or representations which were made not misleading in the light of the circumstances.

Third: That the untrue statements or the omitted facts were what we lawyers call material, and we will get to that for you in just a moment.

Fourth: That the defendant, McDonnell, either knew the material facts were misstated or stated them recklessly and without regard for their truth or falsity; or knew of or recklessly disregarded the existence of omitted facts which if disclosed would have shown that the statements made were misleading.

Fifth: That in the case of an untrue or misleading statement of fact, that that particular plaintiff relied on it. Obviously, there can be no reliance in the case of an omission, and I will take up in a minute the matter of how you feel with a question of an omission.

The sixth element that you must find, the final one is that the plaintiff was damaged as a result of this.

The first element I have already explained. The second element, which must be proved, is that the defendant made untrue or misleading statements of a material fact or omitted such a fact.

Now, misrepresentations are made usually in two ways: First, by a false statement of fact, that is, somebody just tells a lie; or second, they maybe made by omitting or not telling facts which are necessary to make a statement truthful. Misrepresentations may be made by conduct as well as words. They may be made orally as well as in writing.

When one makes a statement of fact, he is obviously under a duty not to lie about it, not to give such a distorted picture or a confusing version that the statement is misleading. Sometimes a half-truth is

no better than a lie, and a fraudulent misrepresentation may be made by a half-truth if it is calculated to mislead. Having chosen to speak, there is an obligation to tell all the facts which are necessary to convey a true and fair understanding of the subject matter.

In the case of an actual misrepresentation, you should consider whether any statement of fact made to plaintiff was false at the time it was made. In this regard, you should realize there is a difference between a statement of fact and a statement of opinion.

A statement of opinion is false only if the person making the statement does not believe what he is saying, that is, that the opinion falsely portrays the speaker's state of mind. That the opinion may have been wrong does not itself render it false. A person can have an opinion which turns out to be erroneous. However, that does not make that expression of opinion false unless at the time the opinion was rendered the speaker did not in fact believe in that opinion.

Plaintiff, Mrs. Murphy, claims actual misrepresentation. She claims that at the end of January or early February 1969, she was falsely told, among other things, by Rick Olney of McDonnell & Company, the subordination of her securities would involve no risk to

her, and she was told also by the company the funds were being used for an undertaking. This is her assertion to you.

Plaintiff James McDonnell claims to you that McDonnell & Company made actual misrepresentations in certain luncheon conferences and in connection with materials furnished him in early 1969 to the effect that the company was in sound financial condition.

All of the plaintiffs, all of the individual plaintiffs other than the trust claim that the defendant McDonnell omitted to state certain alleged material facts. I am not going to recite them all because counsel here have fully and well briefed their positions for you and argued the evidence; but it is claimed that McDonnell & Company failed to reveal such alleged material facts as failure to reveal that McDonnell & Company's violations of the net capital requirements of the New York Stock Exchange; they failed to reveal the fact that they had substantial record keeping problems.

As to the third element, if you find that the plaintiff has proved that one or more of the claimed omissions or misrepresentations of fact occurred, then you must decide whether that fact was material or not. Not every fact concerning a company such as McDonnell is

material.

In determining whether a fact is material you must consider whether a reasonable man under the circumstances in which each of these three individual plaintiffs respectively were situated, if a reasonable man were situated in the position of Mrs. Murphy and Mrs. Anna McDonnell or Mr. James McDonnell at the time and under the circumstances they were acting, would such a person have attached importance to that fact, and might that person have, if possessed and fully informed of this information concerning McDonnell & Company or their investment, acted differently, that is, decided not to subordinate their securities or purchase their stock, as the case may be?

As to whether knowledge or disclosure of any fact affecting the matter might have been considered important by reasonable investors situated as these plaintiffs were at the time they made their investments, the use of the word "might" is intended to convey the concept that it is more likely than unlikely that a certain event would take place or that a decision would have been made in a certain fashion. We use this word every day in our everyday language to indicate something more certain than a mere possibility but not

necessarily an absolute necessity.

As I said previously, you must evaluate materiality in the particular circumstances any given plaintiff was in.

In this regard, defendant McDonnell claims that there is no proof, as to any of these particular purchasers, that one or more of them had any interest in learning the underlying facts concerning the security. McDonnell contends that they were in fact motivated to furnish capital out of a sense of loyalty and obligation to their family and the firm. They quote the statement of Mrs. Murphy, "Don't you trust my family?"

If you find this to be so, this is a factor you can consider in determining whether the facts which McDonnell knew but omitted to disclose to the purchaser were material. If you find such loyalties are what a particular plaintiff really considered important in its transaction with McDonnell, then you may conclude that the claimed omissions were not material in these circumstances even though they might be in other circumstances.

On the other hand, just because family loyalty played some part in plaintiff's investment does not mean that omissions were not material. It is

possible that what might be material under some circumstances will not be material under other circumstances. That is what I am saying.

Nor, I want to firmly state, is the existence of a family relationship between the plaintiffs and certain officers and directors of McDonnell & Company a defense in and of itself to a securities act violation.

Now under rule 10B5 of the 1934 Act, each plaintiff need only prove one material omission of fact or material misrepresentation of fact in order to recover. With respect to a false and misleading representation, there must be reliance. That is the fourth element. As I explained earlier, with respect to an omission, there is no requirement of reliance because obviously no person can rely in reaching a decision upon an omitted fact, because obviously by the nature of the fact that was omitted the person didn't know it and couldn't have relied on it.

Given this inability to make a showing of reliance with respect to an omission, in such cases what is necessary is that you must find, if you are going to find for a plaintiff, you must find that the omitted facts be material in the sense that a reasonable

investor might have considered them important in the making of this particular decision.

In other words, had the person known the facts omitted, he might, in the sense I previously used the word "might," he might not have purchased or subordinated the securities in question.

If you find that McDonnell & Company made untrue statements of material facts or misstated material facts, the test for determining whether a plaintiff relied on an alleged misrepresentation or whether the misrepresentation was substantial is whether the misrepresentation was a substantial factor in the plaintiff making a choice as to whether or not he or she would put money into McDonnell & Company.

You should therefore ask yourselves whether the plaintiff whose claim you are considering was influenced by the claimed misstatement of fact. If it appears the plaintiff already knew the true fact, it has been suggested that the mother, Anna McDonnell knew the condition of the company because she had said she knew that the condition was worse, it is argued to you one way that that is evidence she knew. It is argued to you another way that that is not evidence that she knew, nor inquired.

Or if you find that the plaintiff such as

James McDonnell had already read the October '68 balance sheet with its footnotes, and being aware of that, reposed no confidence in the alleged misstatements of facts, then the false statement cannot be regarded as a substantial cause of that plaintiff's decision whether or not to subordinate securities or to buy common stock, and that plaintiff cannot be said to have relied upon it.

The fifth element requires that even if you find that a particular plaintiff has proved by a preponderance of the evidence that McDonnell made material misrepresentations or omissions to that plaintiff, you must return a verdict for McDonnell unless you find by a preponderance of the evidence that McDonnell's conduct demonstrated wilful, deliberate, or reckless disregard for the truth.

Each plaintiff must prove by a preponderance of the evidence that the defendant sought to be held liable to any charge had actual knowledge of any fraudulent misrepresentation or omission which that defendant made, or that a failure to discover the falsity of the misrepresentation or omission when knowingly made amounted to a wilful, deliberate, or reckless disregard for the truth, or a defendant knowingly and recklessly

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used a scheme to defraud the plaintiff.

In determining whether defendant McDonnell & Company had a wilful or reckless disregard for the truth, your inquiry will be to determine whether the defendant had knowledge that material facts were misstated or omitted and should have realized their significance, or that the defendant failed or refused, after being on notice of a possible material failure of disclosure, to ascertain and disclose such facts when they could have done so by reasonable effort.

The sixth element you must find is the plaintiffs suffered some damage as a result of the claimed material omission or representation. That one I will reserve for later.

If you find that a plaintiff with regard to any of those three claims against McDonnell & Company has established all the elements of his or her claim, then you should return a verdict of liability in favor of that plaintiff against McDonnell.

If, on the other hand, you find that any plaintiff has failed to establish any one of these elements of its claim, you should return a verdict in favor of defendant McDonnell as to that plaintiff on that claim.

Now, with regard to the debenture rollover, still with regard to McDonnell & Company, turning now specifically to the rollover of the series B subordinating debenture which was owned by the trust, which plaintiff trust contends Murray McDonnell wrongly replaced as a McDonnell debenture by a series E debenture rather than paying it off, you must be satisfied that the plaintiff trust has established each of the following elements by a preponderance of the credible evidence:

First, that a particular transaction involved a purchase or sale of the security. I instruct you here that a debenture too is a security for the purposes of rule 10B5.

Second, you must find in connection with this transaction that McDonnell by Murray McDonnell had knowingly engaged or recklessly engaged in an act, practice, or course of business, which operated as a fraud.

Third, that fraud resulted in injury to the plaintiff trust.

Now, I am going to take a break for about five minutes, ladies and gentlemen. We will stand in recess.

(Recess)

(In open court; jury present)

THE COURT: Now, turning to the claims against the stock exchange, the claimants against the exchange allege a different theory of liability, and that is that the New York Stock Exchange violated the provisions of section 6 of the Securities and Exchange Act in discharging their regulatory function with regard to McDonnell & Company.

As is probably clear to you by now, the New York Stock Exchange is a national securities exchange registered with the Securities and Exchange Commission, a government agency known as the SEC.

The exchange had adopted a constitution and rules which were approved by the SEC. The exchange and its rules are subject to surveillance by the SEC. It is plaintiffs' claim that the exchange did not properly enforce its rules, the Securities Act of 1934, and the rules under it with respect to McDonnell & Company.

Section 6 provides in pertinent part for the registration of the national securities exchange with the SEC. The statute requires that as a condition of registration, a national securities exchange shall file with the commission an agreement to comply and to enforce, so far as within its powers, compliance by

its members with the provisions of the Securities Exchange Act and any amendments thereto and any rules or regulations made or to be made thereunder.

In addition to being registered under this section, the exchange must adopt rules "providing for expulsion, suspension or disciplining of a member for conduct or proceedings inconsistent with just and equitable principles of trade."

The statute continues to require that the rules of an exchange must declare that a wilful violation of any of the provisions of the Securities Exchange Act or any rules or regulations thereunder shall be considered conduct or proceedings inconsistent with just and equitable principles of trade.

Plaintiffs allege that the New York Stock Exchange registered as such national securities exchange failed to properly discharge its regulatory functions with regard to McDonnell & Company in at least two ways:

First, that the exchange failed to take appropriate measures to correct violations of the net capital rules.

Second: That the exchange failed to take appropriate action to correct certain record keeping

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and other violations by McDonnell.

Three essential elements are required to be proved in order to establish liability for violation of section 6 as claimed by the plaintiffs.

You must be satisfied that the plaintiffs have established each of the following essential elements by a preponderance of the evidence:

One, that the exchange had reason to believe or suspect that its member was acting in violation of the rules of the exchange.

Two, that the exchange thereafter failed to take reasonable action.

And, three, that such failure to act was the proximate cause of damage to the plaintiff in question.

The first element requires that the exchange had reason to believe or suspect that its member was acting in violation of the rules of the exchange.

The duty of an exchange under section 6 is one of enforcement. That is to say, it has to obtain compliance by its members with the applicable rules as far as is within its powers.

An exchange is not an insurer or guarantor of every injury to customers or investors in one of its member firms. Therefore, you must decide whether the

plaintiff has shown by a preponderance of the evidence that the exchange knew of a violation of its rules by McDonnell & Company, or reasonably should have known in the exercise of reasonable diligence of such a violation before there can be any liability on the part of the exchange.

The exchange can only be liable, I might add, for not enforcing existing rules. It cannot be held liable in this action for inadequacies should you find them in its existing rules or supervision of members' activities.

The only remedy for such inadequacies, if any, is for a party to go to the SEC to compel the stock exchange to enact better rules. In other words, you have to deal with the rules that were in force at the time.

The following is a summary of the exchange's rules and constitutional provisions I believe to be at issue:

Rule 325 establishes net capital requirements for the exchange members which at all material times in this act required that "No member" -- this is of the exchange -- "No member shall permit in the ordinary course of business as a broker its aggregate

indebtedness to exceed 2000 percentum of its net capital," as that latter term is defined and computed under Rule 325; and then it goes on to, "Unless a specific temporary exception is made by the exchange in the case of a particular member or member organization due to unusual circumstances."

Thus, under Rule 325 the exchange is permitted in the case of a particular member organization to prescribe stricter net capital requirements.

Now Rule 342 and Rule 440 generally require the maintenance of accurate books and records so as to assure a source of information fairly reflecting the financial and operational status of the firm, customers, investors and the general public.

Before January 30, 1969, article 862 of the constitution provided that whenever it should appear to the exchange that a member "has failed to meet his engagements or is insolvent, such member shall thereby become suspended from membership."

This has to do with failing to meet its engagements or is insolvent.

After January 30, 1969, the constitution was amended to add that a member shall become suspended from membership if it was in such financial or operating

condition that he cannot be permitted to continue in business with safety to his creditors or the exchange.

Article 14, section 6 of the exchange constitution provides that the exchange, after determining a member was in violation of the constitution or any rule promulgated thereunder, or that a member has engaged in conduct inconsistent with just and equitable principles of trade, may suspend or expel the member.

The second element plaintiff must prove by a preponderance of the evidence is that the exchange, after it knew or should have known of the violation of its rules had occurred, failed to take reasonable action to correct such a violation.

Thus, the stock exchange is accorded substantial discretion and flexibility in interpreting and obtaining compliance with its rules to enable it to deal with a multitude of different and often new problems in a fashion that best serves its members and the public interest.

Therefore, the plaintiffs must show that the stock exchange response was not a reasonable, good-faith effort to deal with a violation of the public interest.

A plaintiff cannot succeed just by showing that the stock exchange did not take the best possible

action under the circumstances, nor can you infer that the stock exchange acted unreasonably from the mere fact that plaintiffs were injured, and you are not to judge this from hindsight. You must judge this from the situation as it existed at the time.

Plaintiff must show that the action of the stock exchange amounted to an abuse of discretion on the part of the exchange.

If you find that the stock exchange reacted in one of several reasonable ways, your verdict must be for the exchange regardless of what in fact happened to the plaintiffs' investment.

If, however, you find that the exchange did not act in a reasonable fashion in regulating McDonnell & Company, you must still find that the plaintiff has satisfied the third element, which is that an exchange's failure to reasonably regulate proximately caused injury to a particular plaintiff. Under the law here applicable, ladies and gentlemen, damage is proximately caused by an act or omission to act whenever it appears that that act or omission played a substantial part in bringing about or actually causing the damage complained of; and it further appears that the damage was either a direct result or a reasonably probable consequence of either the act or the omission.

Stated in other ways, that the exchange's failure to act if you so find, resulted in injury to the plaintiffs or that the exchange --

Stated a third way, that the exchange's breach of duty resulted in damage to the plaintiff that can be traced to the breach.

Now the law does not permit a claimant, plaintiff in this case, to walk away from the opportunity to save himself or herself from loss and then make a claim against someone else to make good the loss. If you find that plaintiff Anna McDonnell or plaintiff Margaret Murphy discovered that McDonnell & Company was in danger of collapsing with a consequent loss of their investment, and that they had an available opportunity to save their investment opportunity by withdrawing it and did not take it, or did not use due diligence to read the instrument to ascertain if such an opportunity was available as it is argued it was, you should return a verdict against them even if you find in all other respects they are entitled to recover.

Now, we are getting toward the close. Let me give you what I would regard as some possible questions for you to ask yourselves. This is obviously not intended to be all-inclusive because I am sure you will have countless of your own that have occurred to you over the several

weeks of trial.

Ask yourselves, what were the facts about McDonnell & Company, and when did they occur? Establish that.

Ask yourselves, when did the stock exchange know or suspect that adverse facts existed either by them being told by McDonnell & Company or by inquiry of their own examiners or from any other source.

Ask yourselves whether the exchange acted reasonably or unreasonably, having learned of these facts ask yourselves whether they were in good faith in their actions, having learned of such facts as you find they learned and when they learned them.

Ask yourselves such questions as what were the responsible officials in the corporation saying at various times? Did they want to go forward, did they not? Ask yourselves why did the plaintiffs here put their money in?

I am sure other questions will occur to you during the course of your deliberations.

Now consider, ladies and gentlemen, my instructions as a whole, as an entirety but do not read into them anything that I have not expressly told you; and consider all the evidence. The fact that I may have referred to some and not other places does not mean that it is not all important or that it is all important. You should consider it all.

A word about deliberating: each juror is entitled to his or her own opinion. Each juror should, however, exchange views with fellow jurors. That's what jury deliberation is all about. Discuss and consider the evidence. Listen to the arguments of fellow jurors, present your individual views, and discuss the case with one another, and consult fairly and openly with one another in the jury room to reach a verdict based solely and wholly on the evidence, if you can do so without doing violence to your individual judgment.

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Each one of you must decide the case for himself or herself after consideration with fellow jurors, but you should not hesitate to change an opinion you may hold which after discussion with your fellow jurors appears erroneous in the light of the discussion viewed against the evidence and the law.

However, if after carefully weighing and listening to all the arguments of your fellow jurors and weighing the evidence you entertain a conscientious view that differs from others, . . . , you are not to yield up your judgment simply because you are outnumbered or outweighed.

Your final vote must reflect your individual conscientious judgment as to how this controversy should be decided as to each claim by each plaintiff against each defendant.

Your verdict must be unanimous in order to reach a verdict on any claim by any plaintiff against any defendant.

In the course of your deliberations you may perhaps desire to have some part of the testimony read, or you may wish to examine exhibits if you find that you are uncertain as to some aspects of the case. You may wish to have some portion of these instructions read back to you if you are uncertain as to anything.

In such a case kindly notify the marshal who will be in charge of you, giving him the note and asking him whatever it is that you wish.

Kindly, in sending such notes to the court, do not state your position on any issue because that is your business and not mine and not these gentlemen here.

Now let me say finally: I remind you of your oath as jurors, and that was that you would without fear or favor to anyone, well and truly try these issues between these plaintiffs and these defendants and a true verdict give based solely on the evidence and the court's instructions as to the law. It is important to the plaintiffs; it is important to the defendants; it is important to you as citizens, and it is important for justice in this country.

Thank you very much.

Now, are there any requests or exceptions?

MR. BEERE: Yes.

THE COURT: All right, we will retire to the robing room.

The jury will stay in place.

(In the robing room.)

THE COURT: All right, Mr. Beabe, any requests or exceptions?

MR. BEERE: Yes, your Honor.

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I respectfully except to your Honor's refusal to charge the 10(b)(5) against the stock exchange.

THE COURT: On the debenture roll over?

MR. BEEBE: Well, I am putting it on the record. 10(b)(5) against the New York Stock Exchange in all respects; controlling persons against the New York Stock Exchange; aiding and abetting against the New York Stock Exchange; the duty of the New York Stock Exchange disclosed under Section 6 as incorporated in plaintiffs' request number 20, and Section 6 contract claim, third party beneficiary.

THE COURT: What is that? Section 20?

MR. BEEBE: Section 20 is the -- I don't have it in front of me.

Do you have that, your Honor?

THE COURT: Yes.

MR. BEEBE: That is the duty to disclose --

THE COURT: I think this is covered in substance by saying, did they act reasonably? You get into much more detail in your Section 20.

In any event, I note your exception.

MR. BEEBE: Then insofar as the charges your Honor just announced, it may have been a slip of the tongue, I don't know, but when you were announcing the various parties and how each is to be treated equally, the New

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York Stock Exchange was not mentioned. The defendant New York Stock Exchange should also be specifically noted as being treated no better or no worse.

MR. BROOKS: It was, your Honor.

THE COURT: I think that is in there in substance.

MR. BROOKS: I think it is.

THE COURT: I said all parties, corporations, and so on.

Go ahead.

MR. BEEBE: Then, in terms of burden of proof, your Honor focused on only the plaintiffs, and I believe the charge would also be appropriate to the extent that the defendants have a burden of proof to meet, that they also must meet it by a fair preponderance of the evidence.

THE COURT: On what issue did they have a burden of proof?

MR. BEEBE: One is that they acted in good faith, as a defense, to whatever they did or didn't do.

THE COURT: On the other hand, don't you have to show that they acted unreasonably and not in good faith? I think it is your burden to show that they abused their discretion, which is to be unreasonable or in bad faith.

All right, I note your position.

MR. BEEBE: Then we have the charge on the

uncontradicted testimony. The way I heard it phrased was that it could be disbelieved even though uncontradicted.

THE COURT: Right.

MR. BEEBE: I would just except to that. I believe it is uncontradicted that it stands.

THE COURT: I don't know that to be the law.

MR. BROOKS: I don't know it to be the law either, your Honor.

MR. BEEBE: Then on a basic point you said that the exchange-- that our claim was that if the exchange failed to regulate and it led to the demise of our clients' loss-- I have no problem with that. But our claim also is that if the exchange had regulated properly our clients would not have made the investments, and I would request that that charge be made.

THE COURT: I will tell you what I will do: I am not going to get into that, but I will tell the jury that they should keep in mind in their deliberations all the claims made by all parties in their summations, because if I start having to pick out every claim that everybody had made, and with a fear of leaving one more of them out, I would be in terrible trouble.

All right, I will do that.

MR. BEEBE: Then, of course, your Honor withdrew

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from consideration the New York Stock Exchange's obligation  
to --

THE COURT: To check the signatures?

MR. BEEBE: As to the debenture -- we don't call  
it a roll over; in our view it is a substitution.

THE COURT: Mr. Beebe, in the interest of time,  
and since I don't want the jury to sit there forever -  
I know the place you are at --

MR. BEEBE: All right, I will just note an  
exception to that.

THE COURT: I thought I had communicated that  
yesterday. I did it in connection with Mr. Stein -- no,  
I did it in connection with the responsibility on the  
misrepresentations, and I know I mentioned it, but I did  
not mention it in connection specifically with the roll over.  
I thought I had stated, but obviously I failed to communicate  
it, and that's my fault, not yours.

Okay.

MR. REEVE: You mentioned that the exchange is  
not an insurer. We never raised the argument that the  
exchange was an insurer.

MR. BROOKS: Mrs. Murphy did in her testimony,  
Your Honor. She said they were under the FDIC.

THE COURT: As a matter of fact, she did. I didn't

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give it for that reason; but that certainly would justify it.

MR. BROOKS: Just that it was raised as a fact.

THE COURT: Well, this is a general instruction to a jury that they are not guarantors or insurers.

MR. REEBE: Then you charged on the opinion, when someone expresses an opinion under 10(b)(5) that it's not a fact. You said that the burden is that the plaintiffs have to prove that the person expressing the opinion knew it was not true.

I would respectfully submit that you should add that if the person didn't have reasonable grounds to find the opinion --

THE COURT: I think I did. I think I went much farther than that. I think I said if the person who made it didn't believe it.

MR. REEBE: Right. I am saying if he didn't have reasonable grounds to believe it.

THE COURT: All right, I didn't seem to say that.

I don't think it makes a particle of difference in the overall picture here.

How do you want me to phrase this?

MR. REEBE: If a person expressing an opinion didn't have reasonable grounds to believe it.

THE COURT: On a violation of 10(b)(5)?

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MR. REEBE: Yes.

THE COURT: An opinion is also a violation of 10(b)(5) if the speaker does not have reasonable ground to believe that the opinion is accurate.

I will give that.

MR. REEBE: Now as to James you charged as to the material he received, but there is, I believe, a gap in the charge as to the material that he was not given, the omissions, half of that equation. I believe you covered it with Anna and Margie, but not with James.

THE COURT: I am not so sure but what that is not roughly covered. It certainly was covered in the argument and it is covered, certainly, in the overall charge, that is, an omission or false statement. He claims he didn't get certain papers.

MR. REEBE: In the charge, the way it came out a little later also on James was that he got this Exhibit J, which is the little Lybrand write-up, and then the way the charge says, it was argued that this did not convey the right information. The argument is much broader. The argument is that a great deal of information was not conveyed to him, which you specifically mentioned as to the others but not as to him. All those same problems, the net capital violations, the partner withdrawing, and so on,

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were not conveyed to him. In fact, your Honor, on the record as it stands right now it clearly was not.

THE COURT: Well, I made the statement -- I know because I read it from here, and I think as to what you are talking about, what I did say was that the plaintiff McDonnell claims that the McDonnell Company actually made misrepresentations in March, 1969, that the company was in sound financial condition. All of the individual plaintiffs but not the trust claim the defendant omitted to state certain alleged material facts, failure to reveal the capital violations, failure to reveal the record keeping problem. I made that statement.

MR. BEEBE: Very well, your Honor, if that's broadly on the record, all right.

Now, I have a few others here.

You summarized the case with regard to Anna, and that is that she knew things were worse. That's very important in that the primary argument is that she was not told all the things that were worse.

THE COURT: But you argued that. I said that was what one side contended, and that was notice to her, and you claim it wasn't. My memory is that is what I said.

MR. BROOKS: You did your Honor.

THE COURT: They say that's notice and you say it

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isn't.

MR. BEEBE: I say it much more fully.

THE COURT: I know, I am only charging on the law; I am not arguing your case.

MR. BEEBE: The only reason I focus on that is that it seems to isolate certain facts without giving the other side of the picture.

Right after the break you were charging about how the exchange had reason -- the burden was whether the exchange had reason to believe or suspect. For some reason the word "knew" was left out, and I think that's very important, because part of the evidence goes to the fact that the exchange affirmatively knew, and that was left out of both phraseologies as to that standard as you announced it.

THE COURT Isn't that in the charges?

MR. BEEBE: In ours it said "knew."

MR. BROOKS: In ours it does too.

MR. BEEBE: No, clearly it does not. We checked that.

MR. BROOKS: How did you check it?

MR. BEEBE: Because we were reading the charge as you went along.

THE COURT: You are right. I shall add that.

MR. BROOKS: How will it read now your Honor?

THE COURT: I shall say that in one of the elements

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I left out the word "knew," and I will read the element to you with that word in it.

I will read all three elements: One, that it knew or had reason to believe or suspect that a member was acting, and so on, and therefore that the failure to take such reasonable action was the proximate cause of the failure.

MR. BEEBE: Thank you.

Now, in reading 325 you read on to the bottom of it about the specific exception.

THE COURT: Right.

MR. BEEBE: As I remember very clearly on the record when this came up at some earlier juncture, Mr. Brooks said "We are not arguing that there was a specific exception here."

I never asked Mr. Bishop any questions about that because I thought that was out of the case. It is out of the case, your Honor.

MR. BROOKS: I don't think it is at all, your Honor.

THE COURT: It is either relevant or it is not relevant. If it is relevant, fine; if it is not relevant, it doesn't make any difference.

MR. BEEBE: I specifically refrained from asking Mr. Bishop because I knew what his answer would be, that we

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didn't make a specific exception, and I didn't ask any questions along those lines in eliciting the testimony.

MR. BROOKS: I asked those questions of Mr. Bishop and he answered they can make an exception.

MR. BEEBE: But they didn't make an exception.

MR. BROOKS: He didn't say that.

MR. BEEBE: I think if we will look back at the transcript -- and this is quite important -- that Mr. Brooks specifically withdrew that from the case.

MR. BROOKS: I didn't withdraw that from the case.

MR. BEEBE: You said "I am not arguing that."

MR. BROOKS: I didn't argue it on my motion, and I am certainly not going --

THE COURT: I think I will let it stand and I will note your exception.

MR. BROOKS: Your Honor, while you are in that area, I think you misread your notes when you were reading at that point. You said the rule provided for an exception under unusual circumstances, and then you went on to say: and thus the exchange could require stricter capital requirements of Rule 325.

I think there must have been a line that you dropped.

It can go either way. You can except or you can

provide stricter requirements.

MR. BEEBE: I think the way it came out was that the exchange could require an exception or could require stricter enforcement.

THE COURT: You want me to read that in the alternative, is that it?

MR. BROOKS: Yes.

THE COURT: To provide a temporary exception?

MR. BROOKS: Under usual circumstances or it can require --

THE COURT: All right, I understand.

MR. BEEBE: Your Honor, I would vigorously oppose a rereading of a charge that I am excepting to because I believe it is in the transcript that Mr. Brooks said "I am stipulating and I am not arguing that an exception was made." That is in the transcript.

THE COURT: Mr. Beebe, I can't resolve that at this point without seeing the transcript, and I have got the jury here and I am going to have to rely on the fact that this is a rule which exists, and either it's relevant or it isn't relevant. It either fits or it doesn't fit. If it fits the fact the jury finds, then it does; if it doesn't, it is irrelevant.

MR. BEEBE: Does anyone else in reading the

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transcript recall what transpired a few days ago?

MR. BROOKS: You are attributing it to me, Mr. Beebe. And I don't recall that.

THE COURT: In other words, Mr. Brooks, on the other hand, is that it, under Rule 325, the exchange is permitted?

MR. BROOKS: It can make it tougher or it can make it easier. The rule so provides.

MR. BEEBE: Maybe I can minimize or try and do something about this exception and this charge that is coming in again by suggesting, your Honor then read at that point that there is no evidence in this case that an exception was made for McDonnell & Company.

THE COURT: I am not going to do that.

MR. BEEBE: I respectfully except to your disposition to do that.

THE COURT: All right, go ahead, because we have got the jury sitting outside.

MR. BEEBE: I have three more.

I except to the standard set forth on the exchange's discretion and the response that the exchange presumably can make.

I except to the language about walking about from opportunities in that charge, and I except unless it

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is corrected in some way to the instruction that the plaintiffs could have withdrawn. I believe that should be, and I would request that it be instructed to them that the jury must find that in reading the instruments and in considering the testimony about the circumstances, that the plaintiffs could have withdrawn before it can find that they were under some duty to do so. I don't think that was said.

MR. BROOKS: I think your Honor said that.

MR. BEEBE: I don't think that was said.

THE COURT: What I said was: If you find plaintiffs, so and so, discovered that McDonnell & Company was in danger of collapsing, and that they had an available opportunity to save their investment by withdrawing and did not take it, or did not use due diligence to read the instrument to ascertain if such an opportunity was available, as it is argued it was, then you should return a verdict against them.

MR. BEEBE: Then may I just ask that also the opportunity -- that it is argued that it was not available, because the way that reads, the phraseology is very affirmative, that an opportunity was available if only they had read the instrument.

THE COURT: It is only applicable if the opportunity

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exists.

MR. BEEBE: The way it reads, your Honor, I think it is so affirmatively phrased that I would request a reading of the converse, too.

It is also argued that the opportunity - something like that - even if they had read it, that such opportunity was not available under the instrument in the circumstances.

THE COURT: I think I will leave that alone.

MR. BEEBE: I just would like a converse reading.

THE COURT: It gets much too complicated, of course then you have got to get into all the other things.

All right, you have an exception.

MR. BEEBE: The last two exceptions are, in the asking yourselves questions series there was one about whether the exchange acted in good faith, and I respectfully except to that, and whether the company wanted at one point to go forward. I don't think that pertains.

THE COURT: All right.

Mr. Brooks?

MR. STEIN: Your Honor, I have two very brief exceptions, with all due respect.

The receiver excepts to the fact that the jury was not given as one of the five elements that plaintiff must establish against the defendant in order to find

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10(b) liability, that the plaintiffs fulfilled the duty of due care by seeking to ascertain the facts relevant to their transactions with McDonnell & Company, and I am specifically referring now to the language in request to charge 13. That should have been an element of their case.

I am specifically referring to the facts in this case about the plaintiff reading material made available to that plaintiff, or whether the plaintiff asked questions that a reasonable person would ask under the circumstances.

I am also referring to the factors that would include the plaintiffs' education, business sophistication and expertise and the access of information generally and the special relationship that the plaintiff had with the defendant.

THE COURT: Your exception is noted.

MR. STEIN: One other, your Honor:

In the charge where you considered the standard of materiality, I believe you gave as the basic test for materiality whether a reasonable man or woman placed in the precise situation of each plaintiff might have acted upon the facts misrepresented or omitted, in determining his or her course of action in the transaction, and I except to the use of the word "might." Rather, the word and the standard should have been "would," and I cite for that a

recent Second Circuit authority where the standard is whether or not the plaintiff would have acted upon the facts misrepresented or omitted in determining his course of action in the transaction in question.

THE COURT: Your exception is noted.

MR. BROOKS: Your Honor, I have no problems with any of the instructions you have given except the one you have corrected, but I would like an instruction that there was an \$20,000,000 contingent liability in McDonnell & Company in November, 1968, and there was no ten days of blank tape on McDonnell's official transactions in November of 1968.

We discussed it this morning about Mr. McDonald's testimony and the other testimony.

THE COURT: Those are fact matters and not law matters, and to the extent that I thought the jury might have gotten a misimpression, I think that was corrected during the course of the argument. So I decline to do that.

MR. BROOKS: I except.

I would like the same instruction that you gave on depositions as to interrogatories, which were a pretty crucial part of James' cross-examination and which I read into the record.

THE COURT: I think I did that when the jury was

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read that. I think I told them what it meant. I am not going to do that now.

MR. BROOKS: You did the same thing with depositions at that time.

THE COURT: I know I did.

MR. BROOKS: And now you repeated it.

THE COURT: I know I did.

MR. BROOKS: I request my short form SEC charge that we discussed yesterday, that the SEC knew about McDonnell, took no action about McDonnell & Company, and therefore you can infer that McDonnell's continuance of business accorded with the Securities and Exchange Act of 1934.

THE COURT: No. In my discussion I ruled out those exhibits on the issue being withdrawn.

MR. BROOKS: I except to that.

I am not sure that we had gotten across to the jury that the exchange does not have the duty of disclosure to these plaintiffs on the facts or to the public in general.

So I request an instruction that there was no duty of disclosure to the plaintiffs on the facts of this case, and that there was no duty to make public the fact that a member organization of the exchange was having

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financial or operational difficulties and was under exchange surveillance, citing the cases I have cited in my request to charge.

MR. BEEBE: I think your Honor charged that at length this afternoon, and that is what, in fact, he wants you to charge again this afternoon.

THE COURT: I am not going to do that.

MR. BROOKS: I except to that.

I think you should instruct them that there is no claim that the exchange's rules are not proper rules.

MR. BEEBE: I would like a lot of charges about--

MR. BROOKS: I am just getting mine into the record.

MR. BEEBE: I am noting my answer to that particular point.

THE COURT: I decline to charge that.

MR. BROOKS: I would like an instruction about the knowledgeability letter.

THE COURT: I decline to do that.

MR. BROOKS: My 32B in my supplemental request to charge.

MR. BEEBE: I didn't argue knowledgeability letter.

MR. BROOKS: But I am afraid we haven't gotten that down as a responsibility of the exchange as a regulator. You have not charged a disclosure case against

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the exchange, but where do you separate duty to regulate and duty to disclose? That would be my 32B second supplemental request charge.

THE COURT: Declined. You may note your exception.

MR. BROOKS: 35A, the charge on the trust fund, that trust funds are usable only at the conclusion of the exchange and no party has any legal claim to trust fund moneys, and I cite Antonucci v. Robinson and Goldberg v. First Devonshire.

THE COURT: I think that's a fact matter which has been fully argued in the summations.

MR. BROOKS: I except to that.

THE COURT: All right.

MR. BROOKS: Thank you, sir.

(End of robing room discussion.)

(In open court.)

THE COURT: Ladies and gentlemen, just a few little additional matters.

It is pointed out to me that when I was citing certain claims the parties made, I may have overlooked other claims the parties made. Just as I instructed you where I may have mentioned certain testimony or evidence, that did not mean that it was not all important, and you should consider it all, similarly, just because I may have mentioned one claim or another of any party does not mean that each claim that the parties have made before you here extensively and well should not be considered by you in your deliberations, and you should consider every claim that's been made whether or not I mentioned it.

Secondly, in reciting to you when an opinion by someone given in connection with the purchase or sale of a security was a violation of Section 10(b)(5), I did not state but I do now instruct you as well that an opinion as given by a speaker is also a violation of 10(b)(5) if the speaker did not have reasonable ground to believe the opinion was accurate at the time it was given.

Finally, to clarify something that I perhaps left unclear, I had summarized for you certain of the rules of the exchange, and I am going to read certain ones again

here so there is no question as to how it is left with you.

Rule 325 establishes net capital requirements for exchange members which at all material times in this action required that, "No member" -- of the exchange -- "shall permit in the ordinary course of business as a broker its aggregate indebtedness to exceed 2,000 percentum of its net capital," as that latter term is defined and computed under Rule 325.

The quote goes on, "unless specific temporary exception is made by the exchange in case of a particular member or member organization due to unusual circumstances."

Then, or alternatively under Rule 325, the exchange is permitted in the case of a particular member or member organization to prescribe stricter net capital requirements. Thus, I want it to be clear that they could make the tough or easier under the rules as they existed.

Finally, in stating to you the elements that the plaintiffs had to prove to establish a liability of the stock exchange under Section 6, I left out a key word. I am going to add that to you now so there is no question about it. In order to find New York Stock Exchange liable under Section 6, you must be satisfied that the plaintiffs have established each of these essential elements by a preponderance of the evidence.

One, that the exchange knew or had reason to believe or suspect that its member was acting in violation of the rules of the exchange.

Two: that the exchange thereafter failed to take reasonable action.

Three: that such failure to act was the proximate cause of injury to the plaintiff.

All right, ladies and gentlemen, you may now retire and begin to consider your verdict.

Before you do so, Mrs. Bivens, I am sorry to say I am going to have to part you from your friends of many days, and you are excused with my thanks for your very faithful consideration of the evidence as we went along.

The remaining six jurors will be in the custody of the marshal who will now be sworn.

(Marshal sworn.)

THE COURT: Before the marshal takes command, have in mind, ladies and gentlemen, you are to report to me on the issues of liability. If you have reached a determination on those issues that will conclude your work that far, as the case may be.

All right. Thank you very much.

(The jury retired to deliberate at 3:05 P.M.)

MR. BROOKS: Should we tender the original exhibits?

THE COURT: That was going to be my request. If you would, get all your exhibits together in some convenient place. I am sure the jury will ask for them, and as far I am concerned, I would suggest that you stipulate that if they are called for, that Mr. Dorsa just send them in without bothering to convene everybody.

MR. BROOKS: That is agreeable to the exchange.

THE COURT: Anybody have any problem with that?

Mr. Beebe, any problem about that?

MR. BEEBE: As long as a record is kept,  
I have no problem.

THE COURT: Yes, all right.

(Recess.)

(4:40 p.m., in open court; jury not present)

(Court's Exhibits 1, 2, 3 and 4 were marked  
for identification)

THE COURT: Gentlemen, I have received a note, and in response to question No. 3, I have written the following reply:

"Madam Forelady: As to your question No. 3 asking for testimony, can you be a little more specific? It would help the reporter in locating exactly what you desire."

MR. BEEBE: We have some solutions to other questions that we have agreed upon.

THE COURT: Fine, but let's get an answer to that one.

MR. BEEBE: The first request was the subordinate agreements. We sent them in. The second request was for Murray's putting in a million plus, what was the date? I don't know if they asked for documents, but they want to know when did Murray put in the million plus. I submit there is none document, this one, just one document, which is PPP dated May 5, 1969, this is from McKay to the stock exchange, "Reference is made to our April 29 letter enclosing documents for a million dollars borrowed by T. Murray." I submit that answers

the question.

MR. BROOKS: I argued, your Honor, that when they said a million plus, since I had argued that they had already put in three pieces which amounted to excess of a million dollars, they also should get Exhibit 000, which shows that on the 19th of May, Murray put in \$650,000 in addition to the million that Mr. Beebe has referred to, and in addition to that, they should also get Exhibit EE1, which shows that Murray on or about March 10, put in \$600,000 of temporary capital.

So, our dispute is we get one of these or two of them. Would you like to look at them?

THE COURT: I would say give all three to them.

MR. BEEBE: Two reasons, one they asked for the million plus. The other, he argued there were only two pieces at the time, quoting Mr. Brooks, that there were two pieces that came in, and those two pieces were the two documents in May, showing a million and then 600,000. That was how the argument went and I am convinced that that is what the jury is referring to. In fact, I believe they are only referring at the million plus which was what they said in their note.

MR. BROOKS: Your Honor, I have my notes right

here. And I argued first, the \$600,000 came in in March and then these other two pieces came in later on.

MR. BEEBE: That is consistent with my recollection.

MR. BROOKS: And that I said that that makes the total of \$2,250,000 in cash that Murray put in the firm in March, April and May '69. That is what I argued. I think you don't have that until you have all three of those exhibits.

MR. BEEBE: That is exactly what I was just saying, that the million plus refers to that one. That is what they asked for. To give them more than that is in effect arguing the case again instead of responding to their request.

MR. BROOKS: How could it be a million plus if that note is only for one million even?

MR. BEEBE: I believe that is what they were referring to as the million dollar deposit. That's what the note said.

THE COURT: I construe that as they want to know when Murray put money in, and I will let them all go in.

MR. BEEBE: The next item that they asked for, according to my scrawled notes, is James' testimony

about the 20,000 in stock, and we are sending back to ask them for clarification on that.

The next item is sort of a two-part question. The dates when James became manager, and I will stop there for a minute, of the Detroit branch. Mr. Brooks has proposed and I have agreed that we take Exhibit 16, which is James' claim in Delaware, and read paragraph 2 from that, which tells the story of his becoming manager.

THE COURT: All right. That sounds good.

MR. BEEBE: The second part of that was they asked when James bought -- to the effect of when did James buy his stock. That isn't an easy question. And so what we have are a series of exhibits showing, at least in the documents here, what the chain of that history was.

Each of us construed them differently, and since we have a jury here to decide fact, one thought is to give them these exhibits.

THE COURT: All right.

MR. BROOKS: As the answer to that question.

MR. BEEBE: Or as a hint to the answer.

THE COURT: It's somewhere in those exhibits.

MR. BROOKS: Yes.

MR. BEEBE: Or in the testimony as they

recall it. This will help them along.

The last thing is the index of the documents, a very salutary request on their part, which caused us more problem than anything else because we didn't have one document that did all this, so what we did was we took Mr. Brooks' list of the plaintiffs' exhibits, that is his list of our exhibits, and chooped that up a little bit. He had the best list going. I think. And put that in, and that is to the credit of Ms. Lichstein and Ms. Solomon and Mr. Adelson.

In any case, they put together three lists, one of our exhibits, one of their exhibits, one of the short list of receivers' exhibits which we are thankful to them for having drawn up, and we are in agreement to give it to them.

THE COURT: All right.

MR. BROOKS: Mr. Dorsa questioned whether we should mark those indices as an exhibit for identification or not. We have no position on that.

THE COURT: Mark them as a Court's exhibit.

(Court's Exhibit 5 was marked for identification)

THE COURT: Now, I have prepared a sheet of paper reciting the nine claims. I do not have annexed

to it a one or two-word description. I have prepared this with the idea that it might be of some help just to have them listed. We have prepared copies to hand around. I was thinking of putting a one-word description perhaps next to them.

I gather that I made an error in my description of the claims, in that I had misunderstood that the father's preferred stock was an asset of the trust, but apparently it is not.

MR. BEEBE: It's of the estate, sir.

THE COURT: It's of the estate.

Then I made a mistake in my recital of what the claims were. This could correct that, of course. I was going to suggest that, given their desire for some identification, if we could put next to like the very first one, put "dash subordinated debenture."

Same with the second.

MR. BEEBE: "Subordinated loan."

THE COURT: "Subordinated loan."

Same with the next one, "common stock."

Trustees of James McDonnell would be the debenture, the rollover.

MR. BEEBE: Series B debenture.

THE COURT: Series B-E debenture. Let me

do that in ink right now. In all the next five would be "failure to regulate," "alleged failure to regulate."

MR. BEEBE: Maybe there is more on your sheet than mine.

(Court Exhibit 6 was marked for identification)

MR. BROOKS: Satisfactory, your Honor.

THE COURT: I think that is enough of an identification.

MR. BEEBE: The problem I have with it the way it's structured here is that it gives an allegation in the second one, and it describes the --

THE COURT: -- instrument in the first.

MR. BEEBE: Couldn't we say in the second one, "alleged failure to regulate with regard to above transactions"?

MR. BROOKS: It's more than that.

THE COURT: It's with regard to the whole firm.

MS. LICHSTEIN: Why in the first section don't you put "alleged fraud claims"?

MR. BROOKS: Your Honor, Mr. Stein has made a good point, I think; that the alleged failure to regulate should go on to say "McDonnell & Co.," "alleged

failure to regulate McDonnell & Co."

THE COURT: "Inc."

MR. BROOKS: Yes.

How can we read paragraph 2 to the jury?

MR. BEEBE: Bring them back and read it.

THE COURT: Mark out for me with paperclips  
and maybe pencil marks what you'd like me to read.

MR. BEEBE: We can just give it to his  
Honor.

MR. BROOKS: Take the exhibit and read  
paragraph 2.

MR. BEEBE: It's paragraph 2 starting on the  
first page and going over to the second, and for con-  
venience, just read the whole thing. It's not very long.

THE COURT: Just paragraph 2?

MR. BROOKS: Yes.

THE COURT: All right.

MR. BEEBE: Those are the -- maybe it would  
be more convenient if we -- when they came in, just tick  
off each of the questions, and at that point hand them what  
it is that they are asking for or read paragraph 2 or  
whatever it is instead of lumping them all together.

THE COURT: I think that is appropriate.

(Recess)

(In the courtroom in the absence of the jury.)

THE COURT: Now, there is a note on my note.

MR. BEEBE: I think we solved that too.

THE COURT: Now this note asking for my charge as to the father's estate, I am going to state that this is only asserted as a claim against the stock exchange on the theory that it was destroyed in value by reason of the alleged failure to supervise, failure to regulate, and then I will read the essence of the sixth claim, which is only about seven lines.

MR. BROOKS: Can you somewhere, your Honor, cover the point that this stock had been held long before 1969?

THE COURT: I don't think there is any question about that.

MR. BEEBE: I don't think there is any real question about that. I have no problem with that.

Now, on Court's Exhibit 6, can I ask you something about that? The way it is cast, the bottom talks about what is alleged and the top does not.

We lawyers are all familiar with 10(b)(5), and with us it is a kind of magic word, and we know what it means. I would suggest that we put down at the bottom of the part about McDonnell & Co., alleged fraud by McDonnell & Co.

MR. BROOKS: It's all right with the exchange.

MR. STEIN: I have no objection.

MR. BEEBE: Perhaps little footnotes at the end  
of each line.

THE COURT: I did.

MR. BEEBE: You did?

THE COURT: Yes.

All right, let's get the jury.

(The jury entered the courtroom.)

THE COURT: Now ladies and gentlemen, we have  
an exchange of correspondence which have been marked  
Court's Exhibits 1 through 4.

In response to 1, you have received the subordination  
agreements.

They will now be presented to you three exhibits  
having to do with the money of Murray McDonnell into  
McDonnell & Company.

With regard to your third question as amended,  
which is the document which requires James McDonnell to  
buy stock in McDonnell & Company, I understand you have  
received certain exhibits that satisfy that requirement.

MR. BEEBE: Yes, among them is one that satisfies  
another request which pertains to, I believe, what it was  
that required James to make the investment to buy the stock.

and I am referring particularly to Exhibit 17.

THE COURT: All right.

Now, with regard to the date that James became manager of the Detroit branch, and when he was asked to buy stock, the parties have agreed that I shall read to you paragraph 2 of Exhibit 16 which was the claim of James McDonnell, Jr.

Paragraph 2: After initially rejecting the offer to assume management of the company's Detroit office for personal reasons, the claimant-- that is James McDonnell, Jr. -- at the urging of Morgan McDonnell reluctantly agreed to accept the position, and so informed Morgan McDonnell on March 10, 1969, and J. Murray McDonnell, president of the company, on March 18, 1969.

On March 20, 1969, the company informed its Detroit employees that the claimant -- that is Mr. James McDonnell, Jr. -- would become the new manager of the office, and on April 14, 1969, the claimant assumed the responsibilities of office manager.

Now, you have asked for my charge summarizing all complaints.

In response to that, half in anticipation and half added since your note, I have prepared a document marked Court's Exhibit 6. That has on it the nine claims

as identification for you as to what they are. I want to make one correction in my charge, however. I had stated to you, erroneously, that the preferred stock of James McDonnell, Sr. was an asset of the trust, you may recall. I was in error in that. It was not an asset of the trust; it was, in fact, an asset of the estate of James McDonnell, the father, and you will find that as claim number 5 as against the stock exchange.

Further I think it is fair to state in that connection that this claim clearly is not asserted against McDonnell & Company, and that the stock involved had been in this estate for some substantial number of years prior to the events that we are principally involved in here.

So I give you Court's Exhibit 6 for that purpose.

Now you finally asked me for my charge on the roll over of the debenture and the stock from the father's estate.

Now with regard to the roll over of the debenture, I will read to you what I read during the charge proper. This is with regard only to McDonnell.

Turning now specifically to the roll over of the Series B subordinated debenture owned by the trust created under the will of James F. McDonnell, which plaintiff trust contends Murray McDonnell wrongfully replaced as a

McDonnell debenture by a Series E debenture rather than pay off, you must be satisfied that the plaintiff trust has established each of the following elements by a preponderance of the credible evidence:

1. That the particular transaction involved a purchase or sale of the securities. I instruct you that a debenture, too, is a security for this purpose.
2. That in connection with the transaction that McDonnell & Company by Murray McDonnell has knowingly or recklessly engaged in an act, practice or a course of business which operated as a fraud;
3. That the fraud resulted in injury to the plaintiff trust.

Those are the elements there.

Now with regard to the stock in the father's estate, that claim is only asserted against the stock exchange under the alleged failure to regulate, and I will read to you the elements of that. That is this Section 6 claim, and it is under these instructions. I will read you these instructions again:

In order to find the New York Stock Exchange liable for Section 6, you must be satisfied that the plaintiffs have established each of these essential elements by a preponderance of the evidence; and that means that as

to the stock this particular plaintiff, to wit, the estate of James F. McDonnell, as established by a preponderance of the evidence:

1. That the estate knew or had reason to believe or suspect that its member was acting in violation of the rules of the exchange.

2. That the exchange thereafter failed to take reasonable action.

3. That such failure to act was the proximate cause of injury to the plaintiff estate in this case.

Now you may retire to continue your deliberations.

MR. BEEBE: Excuse me, sir, the indexes?

THE COURT: Oh, yes. The parties have prepared the indexes to exhibits which is Court's Exhibit 5, and that is handed you as well.

(Exhibits handed to jury.)

(The jury left the courtroom.)

THE COURT: May I suggest we quit at 6 o'clock.

Anybody opposed?

MR. BEEBE: Complete agreement.

MR. BROOKS: That's fine.

THE COURT: Very good.

MR. BEEBE: Thank you, sir.

(Recess.)

(In the courtroom in the absence of the jury.)

MR. BEEBE: May I have the reporter please read back the charge that your Honor just reiterated for the jury? The area we are particularly focusing on is whether the charge as read again to the jury appeared to take away all claims relating to the exchange's responsibility for the debenture, including the Section 6 claims.

MR. BROOKS: It has no responsibility other than the Section 6 claims.

MR. BEEBE: I know, and the way it read is -- the charge as reread to the jury related only to McDonnell & Co., the way we just heard it.

If the reporter would read it back.

(Portion of supplemental charge referred to read as follows:

"Now, you finally asked me for my charge on the roll over of the debenture and the stock from the father's estate.

Now with regard to the roll over of the debenture I will read to you what I read during the charge proper. This is with regard only to McDonnell."

THE COURT: This is only on the fraud.

MR. BEEBE: Is that what the question was related only to, because the way it comes out there, it appears

to say that the only charge on the roll over is --

THE COURT: Well, let's send a note, because I think we can probably clarify it, because the charge that I read had to do only as to McDonnell as to the fraud.

MR. BEEBE: I understand that, your Honor.

THE COURT: Suppose I were to send in a note that nothing in my recent reading to you withdraws claim 9 from your consideration with regard to --

MR. BEEBE: It is claim 8, pertaining to the roll over and the stock exchange.

THE COURT: Roll over and the stock exchange.  
All right.

"The claim of the trustees against New York Stock Exchange for the value of the debenture on claim 8 is not affected by any supplemental instruction I have given you."

All right, mark this as Court's Exhibit 7  
and send it in to the jury.

(Marked Court's Exhibit 7.)

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(6 P.M. in the courtroom in the presence  
of the jury.)

THE COURT: Ladies and gentlemen, I think it might be appropriate that we recess for the day.

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JURORS: We were just going to write you a note.

THE COURT: Very good. We will recess until 10 in the morning.

Now at that time will you please go directly to the jury room. It is obviously important, particularly at this point, that you don't discuss this matter with anyone else because you are at a critical phase where you will be deliberating only with each other, so do not speak to anyone about this until all six of you are together again tomorrow. So wait on your deliberations until all six of you have arrived, and then please resume where you left off.

Be here at 10 in the morning.

(The jury left the courtroom.)

THE COURT: I am going to pick a jury in a criminal case starting at 10:30. I would assume that you gentlemen and ladies may profitably use your time elsewhere until 10:30, so suit yourselves. The jury will meet at 10.

MR. EEEEEE: We are going to stick all the exhibits and things in the witness room and lock them up, but we will be back before your next trial starts which should be before 10:30 in the morning.

THE COURT: All right. Good night.

(Adjourned to May 22, 1975, at 10 A.M.)

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MARGARET MARY MC DONNELL MURPHY, et al.

vs.

71 Civ 461  
71 Civ 1940

MC DONNELL & CO., INC., et al.

May 22, 1975

Trial resumed.

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(In the robing room)

THE COURT: Just so the record has a little introduction, I invited you gentlemen to discuss with me a damage charge, should it become necessary, given the problems that I and my clerks had last night in having ruminated over this for a couple of days and trying to arrive at charges that are both applicable to the facts, taking conjecture out of the picture, and give the jury some standard appropriate to this situation to guide them.

I want to observe that Mr. Beebe's proposed

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charge on behalf of the plaintiffs, in essence, an all or nothing charge, that if there is damage, the entire diminution of the asset is chargeable on damages, since the charge in essence asks for a determination of the value at the time it was subordinated or otherwise to be compared with its value today which, in effect, is that a claim has been presented and not paid.

Mr. Brooks, on the other hand, for the stock exchange, takes the position that the jury should be given the charge that it is the value of the item that is loaned or otherwise as compared to the value of what the lender or subordinating lender, or so on, actually got, which in effect is saying discount it for the risk factor as of that point of time.

Am I roughly correct in that, Mr. Brooks?

MR. BROOKS: Yes.

THE COURT: This is complicated by the fact that there is very little law to guide us here, with no cases reaching the stage to assist us.

I will tell you what I have in mind to do and then I will open the floor for you gentlemen to give any thoughts or corrections or whatever.

I had in mind to let you work up what your contentions are the jury could find from the evidence

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in this case as to how and when it occurred, what facts give rise to it and what facts bear upon its size.

As an example of that, Mr. Brooks might want me to say to the jury "If you find that the stock exchange improperly regulated it but that Mrs. Murphy could have gotten her money out in the summer of '69 at some discounted price that they must take that into account."

The problems I see with that is that I don't really see any proof in this record as to what she could have gotten it out at. It is possible they could find she could have gotten it out, but what could she have gotten it out at.

If you follow that along, we get to the problem that if they find that and are unable to reach a value as to what she could have gotten it out at, has the plaintiff failed in its burden of showing what the damage is and must the plaintiff come away with nothing. Must I charge it you cannot make a determination on that, the plaintiff failed in its burden?

These are all matters my worthy clerks and I hacked at in the underbrush for several days here.

I had in mind to suggest to the jury various fact alternatives they might consider in bearing upon damages, when it started, when it finished, what is its limits, what are the alternative limits, and then I was going to read to them three standards, all relatively short.

One is the following, which is the proximate cause type statement, and it is entitled "To recover actual damages but no more," if you find plaintiff is entitled to recover on any given claim render a verdict to justly and fairly compensate for the plaintiff for the loss proximately resulting from the breach of duty and not to award damages unless sustained by a preponderance of the evidence, damage proximately caused by statement or omission, or it might be failure to regulate when it appears, that the breach of duty played a substantial part in bringing about and actually causing damage and the damage was a direct result or a reasonably probable consequence, etc.

Then we have the two standards I read yesterday from other authorities, that you can award only damages that can be traced to the breach, or as phrased a third way, damages that resulted from the failure to act, and I am toying with the thought of the

case of Seller against Bow, which had such a statement in it.

To sum up, my thought was to get into this a suggestion of a fact recital and then to lay down these black-letter law standards and let the jury have at it.

Now, this is subject of course to review in case they went overboard, but I would be pleased to have anybody give me anything that commends itself more, and there may well be things. As I say, this is a very thorny thicket.

Mr. Beebe, go ahead.

MR. BEEBE: As I sit here, the first thoughts that come to mind, I would like a chance to glance over a few things I have in the other room, but Your Honor charged on the liability question what I called the walk-away charge, that if you found they could have walked away, then you can't find that the defendants are liable.

Let's focus particularly for the moment on Mrs. Murphy: If she could have walked away, then plaintiffs failed to meet their burden and they can't award for them. That gets around the question of whether we met our burden of proof -- I am assuming they come back with a liability finding -- whether we

met our burden of proof showing there were damages.

THE COURT: Oh, yes.

MR. BEEBE: Therefore, the burden shifts and we have then shown damages and it is a question of how much damages we have shown. If they can then show that if they had come forward with some proof to show that at a given point in the summer she could have blown the whistle, got down to a hundred days, which would have taken her into the fall and got down to, say, \$50,000 for her \$280,000 investment, they could then reach whatever conclusion they would on that score.

The trouble with that is they didn't introduce any such evidence and the jury would be just pulling numbers out of the air to show what she could have gotten away with, and the minimizing of damages is always the burden the fellow who is liable for the damages, he has to show he minimized or took reasonable steps to minimize or what would have happened if she took steps to minimize. I think the burden is then on the defendants to show whatever minimization they could show. The jury will have already crossed the hurdle.

THE COURT: The burden is always on the plaintiff to establish every aspect of his case and damages is one aspect of his case.

MR. BEEBE: Once they get over the liability hurdle, they will have found she couldn't walk away --

THE COURT: You are saying you still have the burden to show it is all or nothing, but they have the burden to show it somewhere in between?

MR. BEEBE: That is exactly right.

Once you have established fraud, as I remember the vague -- and I don't know the black-letter law by recollection, but as I remember, once you establish liability, the damages that flow are whatever a jury could reasonably find from the evidence adduced. Basically, I am saying you have gone a long way once you establish the fraud.

THE COURT: In this Levine case, treating Mrs. Murphy as a buyer of a security, the number one ground of damage is the basic difference between what she paid for it and what she in fact got.

As I understand it, Levine goes on to say you can have consequential damages, but Seller says before you can get that you to have very clear, convincing proof of the consequential damages.

MR. BEERE: This is right off the top of my head: If a guy comes in or a lady comes in --

THE COURT: "A great deal of certainty" is the phrase.

MR. BEEBE: Once you have fraud established inducing the person to come in and the day she came in the door the interest instead of being worth \$280,000 is worth \$150,000 and between then and the time it became worthless it slowly depleted in value and it is hard to see the decline of the stock market, further frauds, or what happened that led to the further diminution of value.

Let's also assume that she was locked in at that point and that the jury has made a finding to that effect by coming back and saying she is liable. Once she is locked in, having been induced in by fraud, it seems to me the burden is on the defendant, if such a burden could ever be met, to show why the defendant is not responsible for the diminution in value in a situation she couldn't get out of.

THE COURT: I think I understand the general thrust. Anything more?

MR. BEEBE: That was very poorly phrased, I must say.

MR. BROOKS: If you take the most common case of fraud, somebody buys a stock on the basis of a

prospectus and press release and on the basis of the prospectus the stock price is 50 and when the disclosure comes out and the company was suppressing and it is really a \$40 stock, then the damages are \$10, but the plaintiff holds the stock and a year and a half later the company goes bust or other reasons, I don't think the plaintiff is entitled to claim that as a result of that fraud she has lost her whole investment, all she is entitled to is the \$10.

When you talk about getting out, I think when the plaintiff knows of the fraud -- take our case -- there are lots of ways she can get out other than by exercising the 100-day demand.

For instance, she could bring arbitration proceedings, could have sued, could have come to the stock exchange and say "These people have done this to me, help me, call the SEC, get me restitution."

I don't think it is just limited to her agreement, although we have argued that because it is in evidence.

I think there are obligations on the part of the person who realizes they have been defrauded, if that be the case, to seek whatever avenues there are available to extricate themselves when they learn they have been

defrauded.

MR. BEEBE: My answer to that is first we don't have the common garden variety of buying a publicly traded stock. The big gap is that it is not publicly traded stock where she could run down to the exchange and sell. It comes back to the question of whether she can get out in 100 days.

The jury having found that she couldn't walk away, that she was locked in, to give them the second bite of that apple is asking them to find the same thing twice, as if there was a difference in the two. We are presuming if they come back with a finding of liability they will have had to find in the course of that finding she couldn't walk away, because of the way it was charged.

MR. BROOKS: How about all the facilities the stock exchange has available, like arbitration, like a bureau of inquiry and complaints, or the SEC? If a person discovers they have been defrauded, they have to do something about it. They can't ride it out and then come back and say "I lost the whole thing because I was defrauded for a month and then rode it out for another year."

MR. BEEBE: I agree with Mr. Brooks on that

score, that the burden is on the plaintiff -- well, I agree to this extent, that that issue, whether the plaintiff should have done something to get out rather than what she did, whether there was plenty of evidence in there about all the steps that she took to try to get out, and all the things she was told there was no choice -- the Ira Haupt lawyers that came down, and somebody had them advise the company "Don't blow the whistle, don't get out" but that is because, as far as she was concerned, she was in the classic role of a major creditor of a troubled company and she is always on the horns of a dilemma. If he blows the whistle the company goes under and, on the other hand, he says someone tells him, and probably correctly, just stick with it a little while and maybe everything will get better.

I don't think putting a creditor to that burden and then saying later "You made the wrong choice, you should have blown the whistle," I should think that is a pretty heavy burden for the other side to establish she made the wrong choice.

Point No. 2 is the double jeopardy point. This issue has already been tried, all of those were argued to the jury on the liability question --

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THE COURT: The only one argued was that she could get out.

MR. BEEBE: I assume that includes arbitration or whatever other method she could use to get out. It was all before them and you put it in terms of walking away. I don't think it is fair now to say we are going to say she could have gotten out under the terms of the subordination agreement and if you find liability under that you have to make a second finding, that she could have gotten out under arbitration. That is trying the same issue again and again.

MR. BROOKS: I don't think you can assume that has been decided if the jury comes back with a general verdict.

THE COURT: I think the charge I gave was that if they found she had an opportunity to get out and didn't take it they should find for the defendant even though in any respects they were inclined to find for the plaintiff.

MR. BROOKS: One of the things the plaintiffs are asking in the way of relief is rescission and I think the law is pretty clear on rescission, that someone has to take the first available opportunity when they know the facts to exercise their

remedy, otherwise they are estopped.

It is pretty clear, taking Mrs. Murphy as an example, she knew in early spring, when Sandra McDonnell told her the condition of the firm was terrible --

MR. BEEBE: That is not against the stock exchange, we are not seeking rescission against the stock exchange, and rescission, your Honor, is a separate subject on which I happened to do a lot of study a long time ago --

MR. BROOKS: As long as I know they are not seeking rescission against the stock exchange, fine.

MR. BEEBE: That will be true if the jury doesn't give satisfactory results under the law and then comes the equitable issue.

MR. BROOKS: Can I address myself to my problems?

THE COURT: Surely.

MR. BROOKS: It seems to me if they are going to find liability against the exchange for failure to properly regulate, to be able to evaluate the damage they will have to find when that failure to regulate commenced and what damage that failure to regulate caused to the plaintiff's investment.

If they found, for instance, that the failure to regulate started at about the time Paul McDonald said he couldn't liquidate the company and come out with any capital value, then I think they find there was no damage caused by the failure to regulate. If they find the failure to regulate at an earlier time, they must determine how the failure to regulate damaged the plaintiffs and how much, in what value.

THE COURT: You can't say that a failure to regulate that started, say, on June 15 eroded all of the plaintiff's capital without finding that it was all there and available on June 15, and the failure to regulate might not cause the entire loss.

Perhaps when they entered into the reorganization on September 30 there was another opportunity to get out, they didn't have to sign that reorganization document. Margaret could have said "I'll take mine, you fellows can go your own way."

MR. BEEBE: You did three things there and the last one is the one we have already discussed. We also did proximate cause, which I think is found by the time they find liability, but the third point Mr. Brooks was just making I think merits some thought. If a guy fails to regulate back in 1968 and the jury so

finds, it seems to me there are two ways we can be damaged:

We were not informed, the company was in a position where the exchange was conducting a pattern, a course of conduct that resulted in our clients coming into a situation where they didn't know the rules were not being enforced, if I can oversimplify the case, and the second one is that the continued pattern, their continuation of the pattern, caused damage and it is very hard to draw the line as to what moment the whole thing is wiped out.

Once the jury, I believe, finds that there was damage caused by the exchange's failure to regulate going back into 1968, there is no point that the exchange claimed it had changed that plan. It argues it didn't start the plan until the beginning of 1970. If the jury finds liability against the exchange they will have found that the pattern existed and the plan was in place much earlier and, fortunately again, the exchange didn't suspend the plan or stop it or change its position before the McDonnell Company was under.

We don't have the difficult point of the exchange saying in September '69 that they are going to

back and enforce the rules against McDonnell. But that didn't happen. We all have problems and differences of opinion as to when the plan started, but it did start at some point and continued right through the whole thing.

Once the plan was in force and operation, the jury will have found the proximate cause, otherwise they won't be returning liability against the exchange, the way it is charged, and then the only question is how much our clients were damaged -- not whether they were damaged, but how much.

The evidence they put in and the way they argued it was that it had a net worth -- you remember all the net worth figures which were apart from the net capital computation -- and it was \$16 million at the end of January and I don't know if that gives the company, really, any value in terms of a bankruptcy at that time or a liquidation, because its debt structure from the figures in evidence showed an outstanding debt of \$101 million, somewhere in that magnitude, against a capital of around \$20 million.

MR. BROOKS: That is not proper accounting, Your Honor.

MR. BEERBE: I am not pretending I understand--

MR. BROOKS: Assets minus liabilities give you a net worth of 16 million and if you are going to liquidate you have to match that with expenses --

THE COURT: Are you suggesting that I should ask the jury under section 6, assuming they get there, to make a determination as to when they find the failure to regulate began?

MR. BEEBE: Not necessarily. I would be saying more in terms of what they find the consequences of failure to regulate was.

THE COURT: In order to have a rational way to review whether they were operating within the factual and legal framework of this case, we probably should get an answer to that question, should we not?

MR. BROOKS: I would think you have to.

MR. BEEBE: I would think in terms of -- no, I would not agree with that, your Honor, for this reason: If the failure to regulate contributed in some material sense to our clients coming in or they were entitled to rely on the fact that the rules were being regulated in the normal way, then their damage would be complete, it seems to me.

THE COURT: Let's throw out the hypothetical that the jury were to find that the failure to regulate

began after Murphy's last capital contributions in May.

MR. BEEBE: Let's say May. I don't know whether that ties in with Murray or not. Say they find it is in May 1969 --

THE COURT: Well, Murray is keeping the ratio under 2000, more or less, it is argued, up through May and it is after that point that they begin selling off things and the well runs dry, as you argued.

MR. BEEBE: That the money tree wilted.

THE COURT: They started to raise money from other sources, selling things off, selling seats, and this and that.

MR. BEEBE: At that point the jury would have to make a determination whether the value of the asset, in each case the subordinated loan was still what it was when our clients came in and that it thereafter was rendered worthless and that -- they will have already determined that the exchange had accountability for that consequence.

THE COURT: They could find them liable for any decline from that point on.

MR. BEEBE: Your Honor, here you have the value of what each of the investors had put in very

firmly established as of the various dates involved and the records as to the argument the exchange makes, that he company had a lot of net worth and was running along at a good clip and as long as the money tree held up, that was a fine, upright company.

I am sure the jury could conclude that, otherwise you get into the impossible situation of saying that at this point with liability having been found with the exchange being accountable for what it did, somehow a magician has to come in and pinpoint an exact day and an exact dollar value for the various counts at that moment.

I think the jury can from all the evidence reach its own determination on that issue without saying -- you are taking the other extreme, "I want all or nothing" and that would give absolutely nothing carried through to a conclusion, and I don't see that as a fair outcome when you have a finding of liability.

THE COURT: I agree with you, but then the question is how to assist these six people in coming to something that is fair.

MR. BEERBE: Let me think about that in terms of framing the way it should be stated to them.

MR. BROOKS: Perhaps this would be a

subject on which we should propound special interrogatories to have the jury answer as a group.

THE COURT: I am beginning to think that.

MR. BROOKS: I would like to make another point about Mr. Beebe's remarks, where he talks about his client relying and the stock exchange not disclosing, I don't understand that to be under section 620 as charged to the jury, I understand the charge to be that the stock exchange had a duty to regulate and it either fulfilled the duty or it didn't, but there is nothing about disclosure or reliance that enters into the claim against my client before this jury.

THE COURT: So I understand.

MR. BROOKS: We are talking about statutory duty to enforce rules.

THE COURT: What is taken out of the case is not quite what Mr. Beebe is arguing, but I don't think Mr. Beebe is correct even so. I think what you are arguing is that Mrs. Murphy in putting her money in is saying "My money is safe because the exchange will regulate properly."

MR. BEEBE: In the same sense that you, Your Honor, or anyone here puts money in a bank -- this was Mrs. Murphy's thought -- you don't think to yourself

conclusively "Thank goodness there is the federal reserve board and the FDIC" but you know they are there and if it turns out the bank is fraudulently disclosing its FDIC logo then you are damaged by the failure to perform under the rules as they said they were going to do.

THE COURT: Not because you were injured in your expectation of a reliance, you are only injured by the fact of non-performance.

MR. BEEBE: The reason I argue that and I think it was fairly argued is that it meets the question of whether she was motivated and the others were motivated by love of somehow Murray, and so on, or whether they were also feeling very comfortable there because the rules were being enforced.

MR. BROOKS: If they have to prove that reliance, your Honor, I don't think they have. Mrs. Murphy said she thought the stock exchange was like the FDIC --

MR. BEEBE: That is straying a little far afield from the damage question, your Honor.

(Pause)

THE COURT: Let me throw out another alternative: Suppose you were to work up with me a

series of questions that would get at controlling dates and facts as to when certain periods began and ended and what this jury would conclude would be the effect of that, and required them to answer those, without in any way asking them -- this is assuming that it is not an all or nothing situation -- and having gotten those questions answered, to then continue a trial before me with expert accounting proof as to what is involved in such -- in other words, suppose in the summer of '69 the stock exchange is found to have commenced to improperly regulate, they are only chargeable with a certain amount of damage, and you cannot ascertain that on this record, as I see it.

I don't see any way that this jury is in a position to figure what the damage would be chargeable against the exchange from, let's say, June 1, 1969, to the end of the period. It puts them in a position of really an all or nothing situation, and unless they find all, they are going to have to find nothing.

(Pause)

MR. BEEBE: Well --

THE COURT: Let me just finish my thought, Mr. Beebe.

I feel that if the jury were to conclude that your clients were entitled to some damage but not all, the burden, I still feel, is on you to show how much, and if the record doesn't show how much I fear that I would have to charge the jury that you have not met the burden of showing that amount, and then the plaintiff has failed.

Perhaps I am wrong on that, but that is my impression as to this case, and one of the problems here is that we did not have an expert witness testifying as to different alternative effects of things and what would have happened if you had done this and what would have happened if you had done that, and what the value would have been if this had happened, and so on.

MR. BEEBE: To prove that kind of damage, a narrow, narrow line approach to damages would require a moment in time when suddenly the exchange or Mr. Bishop wrote one of their magic memos and explained very nicely that as of this moment in time we are --

THE COURT: Well, it is a question of what the jury finds. Suppose the jury finds that after Murray's

money went in the exchange really wasn't doing its job?

MR. BEEBE: Indeed, we didn't know what the jury was going to find --

THE COURT: Suppose they ask that question.

MR. BEEBE: Then the corollary question is, what was each of the accounts worth at that point, which is something that, of course, we couldn't have proved to them on the trial in chief because we didn't know what the jury, a reasonable jury would come back with in answer to that question.

Even on all the evidence that has gone in right now there are different contentions as to what the answer would be. We would have had to prove that as of each moment during that year and a half cycle, what the value of each of the accounts was, and that would have been horrendous, and I don't think your Honor would have tolerated that kind of proof, alternate damages depending on what you find, whether it is day 1 or day 2, or whether it is after a certain period or before a certain period.

So instead we introduced all the evidence to show what the various accounts were worth; we showed a great deal of evidence as to what the company was worth at different points in time, and we showed what the final worth of the company was, trying to cover every base possible.

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Now, from all that evidence the jury, I believe, can find, even given your hypothetical, that they say it is some time in the summer that the stock exchange suspended enforcement, that the accounts were worth, taking Margie's question as an example, \$282,000 on January 30th or as of February 4th, or whatever it is; and can reach a determination that the account was still worth the same amount in the summer because the funding, the well was still gushing up the funds so the company was still being kept afloat, and was still solvent and was still marching along happily.

That's the exchange's position, and that's what the jury you are saying in a hypothetical would be finding, that everything was being enforced and done in a normal way up to that date, after Murray stopped being forthcoming with his dough.

Then they find that's what her account was worth as of that point, 282.

THE COURT: Well, I think I have planted the seeds here. Why don't you all give some thought to some concrete ideas, and let's see what the jury comes in with, and when they come in with something we will then have to move and reach a determination at that moment and charge further.

MR. STEIN: Your Honor, there is one thing that seems to have come out as being in agreement during the course of our discussion this morning, and that is that the universe of Mrs. Murphy's claim, so to speak, is \$282,000. We say it's less, based on Mr. Olney's testimony and based on one of the exhibits in the case.

But the complaint of this case demands damages of \$400,000, so we have made some progress, it seems.

MR. BEEBE: I don't want to address that right now.

MR. STEIN: We have got to jump that stream at some point if we are talking about damages, because it's arithmetic--

THE COURT: Well, just because Mrs. Murphy said she would like \$400,000 doesn't mean --

MR. BEEBE: I am sure that was including interest, even though the charge says 400 plus interest.

MR. STEIN: I am not so sure.

THE COURT: Well, I wasn't so sure either.

All right, give some thought to this and give some thought as to whether you want me to work up some factual alternatives as being contentions of the parties with regard to the facts, give them the rules of law as I understand them to be, and that they must reach a conclusion without speculation, etc., etc., and on this

record that may be the best we can do.

MR. BEEBE: Right. We will address that and also the question of how much has been put to bed by the time we find the liability issue.

(End of robing room discussion.)

(11:55 P.M. in the courtroom in the absence of the jury.)

THE COURT: Let the record show that the court received two notes from the jury calling for exhibits, which have been marked Court's Exhibits 8 and 9, and they have been responded to.

(Marked Court's Exhibits 8 and 9.)

THE COURT: Now this Exhibit 97, I am going to send a note with it, which will be marked Court's Exhibit 10, reading:

"Madam forelady, this Exhibit 97 is only admitted against McDonnell & Company. You are not to consider it in any way as evidence against the New York Stock Exchange."

All right?

MR. BEEBE: Satisfactory, your Honor.

MR. BROOKS: Satisfactory.

(Marked Court's Exhibit 10.)

(2:20 P.M.)

(Court Exhibit 11 marked.)

(At 2:30 P.M. the jury entered the courtroom.)

THE COURT: I understand you have reached a verdict and you reached it after everybody here had gone to lunch, unfortunately. I am sorry to hold you up.

Now, you have a verdict?

THE FOREMAN: Yes.

THE COURT: What, may I ask, is your verdict?

THE FOREMAN: We have some different numbers, cases. Margaret Murphy versus McDonnell & Company, we hold in favor of the plaintiff.

Anna McDonnell, individually, versus McDonnell & Company, we hold in favor of the defendant.

James McDonnell, Jr., individually, versus McDonnell & Company, in favor of the defendant.

Trustees of James McDonnell, versus McDonnell & Company, favor of the plaintiff.

And in the stock exchange case, we hold for the defendant.

THE COURT: Mr. Clerk, would you poll the jury, please.

THE CLERK: Your verdict was as to the stock exchange case, for the defendant. As to Margaret Murphy versus

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McDonnell & Company, for the plaintiff.

THE FOREMAN: Right.

THE CLERK: As to Anna M. McDonnell individually, versus McDonnell you find for the defendant. As to James F. McDonnell, Jr., individually, versus McDonnell & Company, you find for the defendant.

THE FOREMAN: Yes.

THE CLERK: As to trustees under the will of James F. McDonnell & Company, you find for the plaintiff.  
Is that your verdict?

(Each juror when asked "Is that your verdict" answered in the affirmative.)

THE COURT: Ladies and gentlemen, I am going to ask you to return to the jury room for a few minutes while we determine the charge that will be given to you on the question of damage on the two causes of action that you found in favor of the plaintiff.

(Jury leaves courtroom.)

THE COURT: Mr. Stein, I will have to confer with you. Mr. Brooks is released from further participation in the case.

Mr. Beebe, I will reserve your right to make motions.

MR. STEIN: Your Honor, I take it our rights

are reserved as well?

THE COURT: Yes, absolutely.

(In the robing room.)

THE COURT: Do you want to use what I suggested this morning as a basis for charging them, Mr. Beebe, or do you have some other suggestions?

MR. BEEBE: Your Honor, we would request the measure of damage charge in our supplementary request number 29. I would like to note our exception to the bifurcation of the case on liability and damages.

I would like to, as far as damages against the company are concerned -- I believe a lot of our discussion this morning does not come to bear because the question of timing is no longer an element. It seems to me the question is what was the value of Mrs. Murphy's account when she deposited her funds, what was the value of the Series B debenture when the substitution took place, what are their values now.

In this regard, your Honor, I would first move, as a matter of law, you should direct a verdict. The damages are clearly established from the record. I can give you the precise figures. They are, in the case of Margaret Murphy \$282,000 plus some other dollars, being the net value after deducting the debit that was on her account.

In the case of the trustees, all the evidence points to the value being 318,000, and whatever the precise dollar amounts were as of October 31, 1968. So I will let that motion, as a matter of law, be my first motion on this score.

THE COURT: I think I will submit to the jury that question, particularly given such cases as Levine, which we looked at earlier.

Do you have anything that you wish me to give, aside from your contention as to what the measure of damages should be? I will hear from Mr. Stein as to what his contention is as to the measure of damages, and I will charge the three different statements of the rule, which all adds up, in my judgment to the same rule, but is one that gives the jury in different language a method of assessing the problem.

MR. STEIN: Your Honor, may I be heard?

THE COURT: Surely.

MR. STEIN: I think what Mr. Beebe is speaking about as a concept of damages, a theory of damages, rescission damages, with respect to Mrs. Murphy, at least-- I would ask that the court charge request for charge number 40. I am referring now to the stock exchange request for charge in which we have joined. That would be a charge

on rescission with respect to Mrs. Murphy's claim.

THE COURT: It seems to me that is an equitable issue.

MR. BEEBE: One we have not reached yet.

THE COURT: To ask the jury to make an award--

MR. STEIN: If the plaintiff, Mrs. Murphy is entitled to \$228,000 it seems to me what she is asking for is her money back. That is a money back measure or damages.

MR. BEEBE: Her claim is that she lost everything.

MR. STEIN: If you buy a security and you spend good dollars for a security and the security is alleged to turn out to be worthless and you want your money back, it seems clear you are asking for a rescission. That has to be the damage theory.

MR. BEEBE: If you buy securities and your investment becomes worthless, you are asking for the measure of what you lost.

THE COURT: Well, I will pass that for now. I don't know that I want to ask the jury to determine there should be a rescission. I think that is something for the court to decide.

MR. STEIN: For purposes of the record, then, let me put this in the form of a motion for a directed verdict,

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that the claim of Mrs. Murphy is for a rescission and that being the case, in order to be entitled to a rescission she must prove by a preponderance of the evidence that a demand was made promptly upon the discovery of the alleged fraud, and since the testimony in the case was uncontested that she found out that she had been defrauded in the early spring of 1969 and no demand was made until some time in 1971, when this suit was instituted, then she can not recover on any theory of rescission.

MR. BEEBE: I think Mr. Stein's recollection of what transpired at the trial might be slightly different than those who followed the trial.

There is a great deal of evidence in that Mrs. Murphy demanded to get out, tried to get out, was told she couldn't get out and now that liability is found, the question is only the measure of damages. All of that walkaway issue was put to the jury already.

MR. STEIN: I was not addressing myself to the walkaway issue.

THE COURT: I have noted your thought on that. Mr. Stein, what about the measure of damages, if that is the view you ultimately take?

MR. STEIN: Then I would request that the stock exchange request number 43 and request number 44 be given

to the jury, on page 22 of the requests that we have adopted.

MR. BEEBE: I have no copies of those.

(Document handed to Mr. Beebe.)

MR. STEIN: Your Honor, I wonder about the possibility here of one or two interrogatories on the measure of damages. Question: What was the purchase price paid by Mrs. Murphy on February 4, 1969, for her investment contract, i.e., the subordination agreement. 2, what was the value of the investment contract if McDonnell & Company had certain problems as alleged by the plaintiffs that were not disclosed to her, such as the back office problem, net capital violations -- off the record.

(Discussion off the record.)

MR. STEIN: 3, what is the difference between the purchase price paid on February 4, 1969, and the true value of the investment contract on the day of purchase?

That ties into requests 43 and 44.

MR. BEERE: May I be heard, your Honor?

THE COURT: Yes.

MR. BEERE: We start with the premise that at this point the jury has found fraud, and in the University of Illinois Law Forum, 1972, there is an article on elements of liability and actual damages in Rule 10(b) (5) actions.

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I think we should focus on what we have now, fraud.

"The purpose of the federal securities laws are to protect investors, to insure the quality of information between buyers and sellers and to protect the integrity of the market. In the words of the Supreme Court, 10(b)(5) is not limited to preserving the integrity of the securities markets, though that purpose is included. Section 10(b)(5) must be read flexibly, not technically." I think the point we are at now, the jury has found liability on these two transactions, and the question is what is the fraud measure of damage. That measure is still, as in all damage questions, one of the consequences of the fraud and the jury has already found Mrs. Murphy was locked in otherwise they wouldn't have found liability, the way the case was charged to them, and the only question left is what was the consequence of what happened to her and to the trustees and the jury should measure what the value of their investments were and what the value became after the fraud was committed. They must have found by now that she couldn't get out before the stocks became worthless.

MR. STEIN: Your Honor, I think Levine teaches an entirely different concept in the area of damages in federal securities cases. I think there has to be a damage theory, a basis for finding damages. Either we are

talking about rescission, which is I think what Mr. Beebe is advocating here, or we are talking about calculating damages by taking the difference between the value of the thing purchased, that is, the securities purchased by the plaintiff, and the value of the thing that was exchanged for it. I think we have to look at the investment contract as of the date she purchased it and calculate the difference between what she paid for it as of the date she bought it and its true value.

THE COURT: Mr. Stein, in that regard could the jury on this record conclude that given the fact that she was locked in to a company that was going to go broke that street value was zero, on this record?

MR. STEIN: That what she paid \$282,000, if that is the figure, and I dispute that, on February 4, 1969 -- as of that date it was worth zero?

THE COURT: As of that date, as a practical matter, it was lost. Could the jury conclude that on this record?

MR. STEIN: I am aware of evidence that the company had a very substantial net worth as of that date.

THE COURT: If she couldn't get it out and the company was going to go broke, then its net worth at any given time is irrelevant. I am not saying you are not right,

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but I am saying I have to give this jury some instruction and guidance and I don't think they are foreclosed from concluding she never could have gotten it out.

MR. STEIN: We have to, I think, look at what she was defrauded out of, what was the value of that investment contract as of the date she purchased it.

THE COURT: Well, that is the teaching of Levine and others, which is clearly so.

MR. STEIN: I went up to the 25th floor today and reread Levine and I am convinced that is the measure of damages alternatively to a rescission measure of damages.

MR. BEEBE: I don't think it applies in the case where you have a subordinated agreement which in effect holds the investor prisoner while the assets are eaten out from underneath, if there were any assets extant at the time.

THE COURT: Off the record.

(Discussion off the record.)

(In open court, jury present.)

THE COURT: Ladies and gentlemen, now that you have determined the liability portions of these claims, you have, as I said, one final task, and that is to decide what amount of damages should be awarded to Mrs. Murphy and to the trust as to those plaintiffs who have carried their burden of proof with you as to liability. I am not

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going to repeat what I said in my charge on the various items, but you must carry that with you into these deliberations.

On the issue of damages, under the law a plaintiff is entitled to recover actual damages, but no more. You must render a verdict in a sum of money which would justly and fairly compensate each plaintiff for all loss proximate resulting from the injuries that plaintiff sustained. You are not to award damages for any loss suffered by either of the plaintiffs unless it has been established to your satisfaction by a preponderance of the evidence in this case that such a loss was proximately caused by the statements or omissions or frauds of the defendant in this case. Damage is proximately caused by a statement or an omission when it appears to you from the evidence that that statement or omission played a substantial part in bringing about or actually causing the damage and that the damage was either a direct result or a reasonable probable consequence of the statement or omission.

Damages exclude all speculation, guess work, surmise or conjecture and are limited to compensation.

The first statement of the measure of damage in a case such as this, a 10(b)(5) case, is what is called the out of pocket rule, and that rule is that you are to

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award the difference between the value of what either plaintiff turned over here, in effect, paid for the new security -- the difference between that and the value of what that plaintiff received as of the time of the event which constitutes the sale we discussed earlier. Now, getting down to cases, Mrs. Murphy subordinated \$282,623 worth of securities and got for it a note. You must determine under this out of pocket rule as of the time she did that what note was worth, and you may do that under all the circumstances. How much was that note in fact worth that she received? The trust, in December, unknown to two of the trustees, had rolled over a B debenture worth \$318,622. There was received at the time of that roll over a Series E debenture and you are to determine as of that time what was that Series E debenture actually worth, and the out of pocket measure of damage is the difference between the \$318,622, the value of the B, and the value that you shall find the E had at that time under all of the circumstances of this case.

In addition to this measure of damages, either plaintiff, or both plaintiffs, as you may find, is entitled to any consequential damage that you find with a good deal of certainty was proximately caused by the 10(b) violation. This means the damages that would flow from that.

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In addition to the difference in value that you may find, you may find there is consequential damage, and in this regard I point out to you that you have already determined in accordance with my earlier charge that Mrs. Murphy did not have an available opportunity to save her investment by withdrawing it, and that obviously has a bearing upon consequential damage in this case. Given those instructions, I will ask you to further deliberate on the damages here.

Do either of the parties want to make any requests or exceptions at this point?

MR. STEIN: Yes, your Honor.

(In the robing room.)

MR. STEIN: Your Honor, I would like to ask you to just spell out with a bit more clarity the concept of time here. You charged that the out of pocket rule was that the difference between the value of what plaintiff paid for the new security and what the plaintiff received as of the time of sale, and then you used the language "What was the note worth at the time" and I am going to ask that the jury be given the date February 4, 1969, or thereabouts-- late January or early February--

THE COURT: That was thoroughly covered, Mr. Stein.

MR. STEIN: Then I except to the charge.

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THE COURT: Mr. Beebe, do you feel that I didn't cover that?

MR. BEEBE: No. Also, you reincorporated your earlier charge and I think that is understood by the jury. I have no exceptions, per se. I will give up the 97 cents on the debenture.

(In open court.)

THE COURT: Ladies and gentlemen, I have nothing further to add to my instructions on damages and you may retire to deliberate.

(At 3:45 the jury returned to the jury room.)

(At 4:20 P.M. the jury returned to the courtroom.)

THE COURT: I have your note as to clarification of the charge on trust, and I will have read to you the tail end of the charge.

(Record read)

THE COURT: Does that give you the assistance that you requested?

THE FOREMAN: Thank you. It is a little better.

(At 4:25 P.M. the jury returned to the jury room.)

(4:55 P.M. in the courtroom in the presence of the jury.)

THE COURT: I have a note which will be marked as a court's exhibit announcing that you have a verdict.

Please tell me what it is.

THE FORELADY: We decided that Mrs. Murphy gets \$300,000 in total and the trust, \$350,000.

THE CLERK: Please listen to your verdict as it stands recorded:

You say you find that Margaret Mary Murphy gets \$300,000 and the trust gets \$350,000?

THE FORELADY: Yes.

(Jury polled.)

(Each juror, upon being asked "Is that your verdict?" responded affirmatively.)

THE CLERK: The verdict is unanimous.

THE COURT: Now ladies and gentlemen, may I say that after four weeks of close association, I have appreciated the three days of careful attention on your part and two days of very careful, deliberate consideration.

I noticed particularly - and I have not been a judge all that long; it has only been a couple of years - but I noticed that the things you asked for showed that you were giving detailed consideration to what the problems

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were that faced you, and I regard your verdict as evidence of careful, individual consideration of the problems that were given to you.

I find that on the evidence your verdict is a thoroughly warranted one, and I want to thank you for your very careful and excellent service as ministers of justice.

You are excused. Good night.

(The jury left the courtroom.)

THE COURT: The last note will be marked Court Exhibit 13.

(Marked Court's Exhibit 13.)

THE COURT: Mr. Stein, I find the verdict as to Mrs. Murphy a little puzzling.

MR. STEIN: I find them both puzzling.

THE COURT: I find the verdict as to the trust was consistent with the charge as given in that it permitted a finding of out of pocket plus consequential, and did not accede the total amount of the claim.

Mrs. Murphy's exceeds the total amount of the claim by some -- what? \$18,000?

MR. BEERE: Could I address myself briefly to that?

THE COURT: I don't see any basis for \$18,000 of consequential damages. There may be a motion to reduce

it to \$282,000 plus interest might be in order, but I will leave that for your consideration.

MR. BEEBE: May I also point out that there is basic at least in the following respect that comes to my mind. In her claim in Delaware the computation was made of the highest average value of her stock in the succeeding month, that is, February, 1969, which was substantially higher than the initial value she put in.

So there is that basis.

THE COURT: I would think, in any event, the verdict is supportable to the extent of 282, and my only curiosity was to the 18.

MR. STEIN: Well, your Honor, we will have to consider that, among other things, in the ten-day period allotted to us to make motions.

MR. BEEBE: And may we ask in that respect, your Honor, that the time for motions to be extended a reasonable period?

THE COURT: I will give everybody 30 days for motions here.

MR. BEEBE: Could I ask for 60 days, your Honor, in the sense that there has been a complex trial, and to tell you the honest truth, I plan to take a little time off.

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MR. STEIN: I have no objection.

THE COURT: All right, 60 days.

I have been intending ever since the close of the plaintiffs' case to put on the record the reasons for dismissing the American Stock Exchange, which are very simple, and I intend to get them on the record now.

The basis of it was that the Amex was operating here under rules promulgated pursuant to congressional authority to the SEC, and those rules were approved, and those rules specifically provided that there should be supervision by one agency and not by two.

And they were operating in accordance with those rules. And if there is to be a charge against them, then they have to change the rules, and I feel that any other result would be inequitable for many of the reasons that I gave prior to the ruling when I gave some examples of what would happen if Honolulu decided one thing and Detroit decided another and Philadelphia, Washington and Baltimore decided a third, and they were all inconsistent, and it is for these reasons that I dismissed the American Stock Exchange.

All right.

MR. BEEBE: Your Honor, would you give us the basis for dismissing the 10(b)(5), the New York Stock Exchange before it went to the jury?

THE COURT: I did at the time.

MR. BEEBE: And the basis for the Section 6--  
dismissing as to the Section 6 with regard to the solicita-  
tion of funds?

THE COURT: I think I just found that this had  
to do --

MR. BEEBE: The method used to solicit the funds  
by not at the same time requiring that the defendants, New  
York Stock Exchange, inform people who were being solicited  
of the condition of the company --

THE COURT: I found that they had no duty to do  
that, pure and simple.

MR. BEEBE: I am asking the basis for that finding,  
your Honor.

THE COURT: That is the basis, that they have  
no duty in law.

MR. BEEBE: Your Honor, those dismissals--  
what rules were those dismissed under, if I may?

THE COURT: These were on the law. I don't know  
which rule you specifically have in mind. If they are in  
response to a motion for a directed verdict, they are on  
the law.

MR. BEEBE: I would say, your Honor, and I  
respectfully request that a formal opinion and finding of

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whatever facts your Honor found in order to reach those conclusions be issued so that we may have the findings of fact and conclusions of law that your Honor made.

THE COURT: No, I decline to do that. I think the reasons for my rulings are based on the record, and I made appropriate statements on the record, and the record stands for itself.

I note that Mr. Brooks departed in a hurry.

I want to say to all counsel, and you may pass this on to Mr. Brooks as and when you speak to him, as I am sure you probably will, that I want to thank all of you for your courtesies to each other, to me, and thank you for the excellence of your presentations and faithfulness to your clients that you have demonstrated for over these many weeks. It has been a pleasure.

MR. BEEBE: May I thank you also, your Honor, for your patience and all the trials and tribulations that we went through. As far as the personal relationship is concerned, it has been a pleasure to appear before you.

MR. STEIN: Your Honor, we can stipulate that, and I think Mr. Brooks will stipulate that also.

THE COURT: All right, good night.

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OPINION AND ORDER GRANTING McDONNELL & CO.'S  
POST TRIAL MOTIONS

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[ Doc. 105 ]

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[ CAPTION ]

71 Civ. 461 (R.O.)

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OWEN, District Judge.

Defendant McDonnell & Co. moves pursuant to Rule 59(a) to set aside the jury verdict or, in the alternative, to reduce the damages awarded. Since defendant seeks a reduction in damages, I will treat this as an application under 59(e) to alter or amend judgment.

Plaintiffs argue that this motion is untimely. Under Rule 59, motions must be served within ten days of the entry of judgment. Although the trial concluded on May 22, 1975, final judgment has not been entered pending decision on previously filed motions. Therefore, this motion falls within the ten-day limit established by Rule 59.

At trial, plaintiffs only established out-of-pocket damages which was the value of the securities the jury found to be obtained by fraud. Plaintiffs' evidence did not, as a matter of law, support an award of consequential damages. Defendant therefore seeks

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OPINION AND ORDER GRANTING McDONNELL & CO.'S  
POST TRIAL MOTIONS

to have the damages reduced to the maximum possible out-of-pocket loss that could have been suffered.

I am not "called upon to find different facts from the evidence, but merely to correct the judgment by striking out that portion which was erroneous because it lacked both legal and factual justification. Rule 59(e) is designed for precisely such situations."

Mumma v. Reading Co., 247 F. Supp. 252, 260 (E.D. Penn. 1965). Accordingly, I order that the judgment be altered so that the damages awarded to plaintiff Margaret Murphy be reduced from \$300,000 to \$282,623 and the damages awarded to plaintiffs Anna McDonnell and James McDonnell, Jr., be reduced from \$350,000 to \$318,622. Plaintiffs are directed to submit a judgment on notice in accordance herewith.

SO ORDERED:

/s/ Richard Owen  
United States District Judge

December 5, 1975

ORDER DENYING PLAINTIFFS' POST TRIAL MOTIONS

[ Doc. 195 ]

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[ CAPTION ]

71 Civ. 461 R.O.

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ENDORSEMENT - Murphy v. McDonnell & Co., et al -  
71 Civ. 461

The only issue raised by petitioner which I believe warrants consideration is that the decision of the Court of Appeals for the Second Circuit in Rich v. New York Stock Exchange, CCH Fed. Sec. L. Rep. 195235 (2nd Cir. 1975) -- rendered subsequent to my charge to the jury has made that charge erroneous. I have studied the Rich opinion. I do not believe my charge to be inconsistent therewith. Accordingly, petitioners' motions as to all defendants are denied in their entirety.

SO ORDERED:

/s/ Richard Owen  
United States District Judge

November 18, 1975.

December 18, 1975.

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ORDER WITH RESPECT TO PREJUDGMENT INTEREST

[ Doc. 106 ]

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[CAPTION ]

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71 Civ. 461 (R.O.)

71 Civ. 1940 (R.O.)

OWEN, District Judge

An application having been made for interest on the award of damages in this action, I conclude that interest should be allowed for the period from the time of the fraudulent taking of a plaintiff's property up to and including the date of the order appointing a receiver for McDonnell & Co. Whether an award of interest is appropriate for any subsequent period, I leave to the discretion of the Bankruptcy Court.

So Ordered.

April 22, 1976.

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/s/ Richard Owen  
United States District Judge

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JUDGMENT

[Doc. 200]

[ CAPTION ]

71 Civ. 461 (R.O.)  
71 Civ. 1940 (R.O.)

The issues in the above entitled consolidated actions having been brought on regularly for trial before the Honorable Richard Owen, United States District Judge, and a jury, on April 28, 29, 30, May 1, 2, 5, 6, 7, 8, 9, 12, 13, 14, 15, 19, 20, 21 and 22, 1975, and the Court having directed a verdict in favor of defendant The American Stock Exchange (the "Amex"), by H. Vernon Lee, Jr., Secretary, in 71 Civ. 1940, and in favor of defendant The New York Stock Exchange, Inc. (the "NYSE") on all claims involving allegations of fraud in 71 Civ. 461 and 71 Civ. 1940, and the jury having returned a verdict on the remaining claims as follows:

(1) in favor of plaintiff Margaret Mary McDonnell Murphy against defendant McDonnell & Co., Inc. in 71 Civ. 461, in the sum of \$300,000;

(2) in favor of plaintiffs Anna M. McDonnell and James F. McDonnell, Jr., as Trustees under the Will of James F. McDonnell, against McDonnell & Co.,

JUDGMENT

Inc. in 71 Civ. 1940, in the sum of \$350,000;

(3) in favor of McDonnell & Co., Inc. in  
71 Civ. 461 and 71 Civ. 1940 on all remaining  
claims; and

(4) in favor of the NYSE in 71 Civ. 461  
and 71 Civ. 1940 on all claims;

and on the 25th day of July, 1975, plaintiffs having  
moved in 71 Civ. 1940 for judgment n.o.v. or for a new  
trial against: (1) the Amex as to the claims asserted  
by plaintiff Anna M. McDonnell, individually, and as  
Trustee under the Will of James F. McDonnell, and by  
James F. McDonnell, Jr., individually and as Trustee  
under the Will of James F. McDonnell; and (2) the NYSE  
as to the claims asserted by plaintiff Anna M. McDonnell,  
individually, and as Trustee under the Will of James F.  
McDonnell, and by James F. McDonnell, Jr., individually,  
and as Trustee under the Will of James F. McDonnell; and  
(3) McDonnell & Co., Inc. as to the claims asserted by  
plaintiff Anna M. McDonnell individually, and plaintiff  
James F. McDonnell, Jr., individually; and plaintiff  
having moved in 71 Civ. 461 for judgment n.o.v. or  
for a new trial as against the NYSE; and the Court  
having denied said motions; and defendant McDonnell  
& Co., Inc. on the 26th day of September, 1975, having  
moved to set aside the jury verdict, or, in the

JUDGMENT

alternative, to reduce the damages awarded in 71 Civ. 461 and 71 Civ. 1940, and the Court having filed its Opinion and Order granting said motion on the 5th day of December, 1975; and plaintiff Margaret Mary McDonnell Murphy having sought an award of interest from the 4th day of February, 1969, until the date of the entry of Judgment in 71 Civ. 461 and the Court having determined, by order dated April 22, 1976, that interest shall be awarded from the 4th day of February, 1969, to the 5th day of April, 1971, said latter date being the date of the appointment of the Receiver of defendant McDonnell & Co., Inc.; and plaintiff James F. McDonnell, Jr., as Trustee under the Will of James F. McDonnell, having sought an award of interest from the 31st day of December, 1968, to the date of entry of Judgment in 71 Civ. 1940 and the Court having determined by order dated April 22, 1976 that interest shall be awarded from the 31st day of December 1968 to the 5th day of April, 1971, said latter date being the date of the appointment of the Receiver of McDonnell & Co., Inc.; and on the 25th day of March, 1976, the Court, on the consent of the parties, having ordered that James F. McDonnell, Jr. and Charles E. McDonnell as Executors of the Estate of Anna M. McDonnell be

JUDGMENT

substituted as plaintiffs in 71 Civ. 1940 in the place of plaintiff Anna M. McDonnell, now deceased;

IT IS HEREBY ADJUDGED, ORDERED and DECREED that Margaret Mary McDonnell Murphy is awarded judgment against McDonnell & Co., Inc. in the sum of \$282,623, together with interest thereon from the 4th day of February, 1969, to the 5th day of April, 1971, in the sum of \$45,911.49, totalling \$328,534.49;

IT IS FURTHER ADJUDGED, ORDERED and DECREED that James F. McDonnell, Jr. as Trustee under the Will of James F. McDonnell, is awarded judgment against McDonnell & Co., Inc. in the sum of \$318,622, together with interest thereon from the 31st day of December, 1968, to the 5th day of April, 1971, in the sum of \$53,974.18, totalling \$372,596.18; and

IT IS FURTHER ADJUDGED, ORDERED and DECREED that defendant McDonnell & Co., Inc. is awarded judgment dismissing all the remaining claims against it in 71 Civ. 461 and 71 Civ. 1940; and

IT IS FURTHER ADJUDGED, ORDERED and DECREED that the defendant Amex is awarded judgment dismissing all the claims against it in 71 Civ. 1940; and

IT IS FURTHER ADJUDGED, ORDERED and DECREED that the defendant NYSE is awarded judgment dismissing all the claims against it in 71 Civ. 461 and 71 Civ. 1940.

E N T E R :

/s/ Richard Owen  
U.S.D.J.

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JUDGMENT

Dated: New York, New York  
May 11, 1976

JUDGMENT ENTERED - 5/13/76

/s/ Raymond F. Burghardt  
Clerk

A TRUE COPY  
RAYMOND F. BURGHARDT, Clerk

By s/Ed. Becker  
Deputy Clerk

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